FILED
JUN 6 1991
OFFICE OF THE CLERK

No. 90-727

In The

Supreme Court of the United States

October Term, 1990

ROBERT G. HOLMES, JR.

Petitioner,

vs.

SECURITIES INVESTOR PROTECTION CORPORATION, et al.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

JOINT APPENDIX VOLUME II

JACK I. SAMET*
Counsel of Record*
JOVINA R. HARGIS
STEPHEN K. LUBEGA
BUCHALTER, NEMER, FIELDS & YOUNGER
601 So. Figueroa Street
Suite 2500
Los Angeles, CA 90017-5704
(213) 891-0700
Counsel for Petitioner

G. ROBERT BLAKEY*
Counsel of Record*
NOTRE DAME LAW SCHOOL
Notre Dame, IN 46556
(219) 239-5717

STEPHEN C. TAYLOR
MARK RIERA
SHEPPARD, MULLIN, RICHTER & HAMPTON
333 So. Hope Street, 48th Fl.
Los Angeles, CA 90071
(213) 620-1780
Counsel for Respondents

Petition For Certiorari Filed November 1, 1990
Certiorari Granted April 22, 1991

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

HONORABLE A. WALLACE TASHIMA,
JUDGE PRESIDING

SECURITIES INVESTOR PROTECTION CORPORATION, et al., Plaintiffs, vs. SEYMOUR VIGMAN, et al., Defendants. AND CONSOLIDATED ACTIONS.	CERTIFIED COPY Case No. CV-83-4742-AWT Consolidated Cases CV-83-4742-AWT (TX) CV-83-5674-AWT (TX) BK NO. SA85-00083-PE ADV. NO. SA85-0138-PE

REPORTER'S TRANSCRIPT OF PROCEEDINGS

LOS ANGELES, CALIFORNIA

MONDAY, OCTOBER 24, 1988

XAVIER MIRELES, CSR 5001
Official Court Reporter
429-D U.S. Courthouse
312 North Spring Street
Los Angeles, Calif. 90012
213/629-7928

[p. 2] APPEARANCES:

For the Plaintiff SIPC:

SHEPPARD, MULLIN, RICHTER & HAMPTON
BY: STEPHEN C. TAYLOR
333 South Hope Street
48th Floor
Los Angeles, California 90071

For the Plaintiff RANDALL CAIN:

WOLF, POPPER, ROSS, WOLF & JONES
BY: LESTER L. LEVY
845 Third Avenue
New York, New York 10022

- AND -

CORINBLIT & SELTZER
BY: JACK CORINBLIT
3700 Wilshire Boulevard
Suite 820
Los Angeles, California 90010

For the Trustees:

JONES, BELL, SIMPSON & ABBOTT
BY: ROBERT A. GRAHAM
800 Wilshire Boulevard
Suite 500
Los Angeles, California 90017

For the Defendant EISEMAN:

COLODNY, FASS & TALENFELD
BY: JOEL S. FASS
626 N.E. 124th Street
North Miami, Florida 33161

[p. 3] For the DASH Defendants:

BLANK, ROME, COMISKY & McCAULEY
BY: LEONARD DUBIN (NOT PRESENT)
1200 Four Penn Center Plaza
Philadelphia, Pennsylvania 19103

- AND -

FRANDZEL & SHARE
BY: STEPHEN H. MARCUS
8383 Whilshire Boulevard
Suite 400
Beverly Hills, California 90211

For the Defendants HABER, HABERICO, HABERS, INC., etc.:

FEINSTEIN, GOURLEY, MALEK & BURSTEIN
BY: STEVEN GOURLEY (NOT PRESENT)
11111 West Olympic Boulevard
Suite 300
Los Angeles, California 90064

For the Defendant JOSE CAMPRUBI SALA:

ROBERT C. GEBHARDT (NOT PRESENT)
2100 Salzedo Street
Suite 302
Coral Gables, Florida 33134

For the Defendant CREDIT BANK [sic]:

GREENBERG, TAURIG, ASKEW, HOFFMAN,
LIPOFF, ROSEN & QUENTEL
BY: DAVID L. ROSS (NOT RESENT)
1401 Brickell Avenue
Penthouse 1
Miami, Florida 33131

[p. 4] For the Defendant MAGNETIC TECHNOLOGIES:

HENNIGAN & MERCER
BY: JAMES W. MERCER (NOT PRESENT)
611 West Sixth Street
28th Floor
Los Angeles, California 90017

For the Defendants NETTIE and SEYMOUR VIGMAN:

HOCHMAN, SALKIN & DeROY
BY: MARTIN N. GELFAND
9100 Wilshire Boulevard
West Tower – Seventh Floor
Beverly Hills, California 90212

For the Defendant AERO SYSTEMS, INC.:

LEE HUSZAGH (NOT PRESENT)
330 Alhambra Circle
Coral Gables, Florida 33134

- AND -

KINDEL & ANDERSON
BY: STEVEN P. RICE
555 South Flower Street
26th Floor
Los Angeles, California 90071

For the Defendant EDWARD P. PRESCOTT:

SHELDON M. JAFFE
1888 Century Park East
Suite 2100
Los Angeles, California 90067

[p. 5] For the Defendants AEROSONIC CORP., FRANK and GOLDMAN:

KINSELL, BOESCH, FUJIKAWA AND TOWLE
BY: DAVID A. PASH
1875 Century Park East
Suite 1600
Los Angeles, California 90067

- AND -

KIRPATRICK & LOCKHART
BY: JOSEPH J. BRIGATI (NOT PRESENT)
1800 M. Street, N.W.
South Lobby
Washington, D.C. 20036

For the Defendant BLUMENTHAL:

KIRKPATRICK & LOCKHART
BY: JEFFREY ALLEN TEW (NOT PRESENT)
100 Chopin Plaza
Suite 2000, Miami Center
Miami, Florida 33131-2305

- AND -

McKITTRICK, JACKSON, DeMARCO & PECKENBAUGH
BY: CARLA L. BELL (NOT PRESENT)
4041 MacArthur Boulevard
5th Floor
Newport Beach, California 92660

For the Defendants TALINGO CORP. and TULA CORP.:

LAMAR, LAMAR & ASSOCIATES
BY: MARIO LAMAR (NOT PRESENT)
3971 S.W. Eighth Street
Suite 505
Miami, Florida 33134

[p. 6] For the Defendants McNEIL and DIAMOND:

LATHAM & WATKINS
BY: HUGH STEVEN WILSON (NOT PRESENT)
555 South Flower Street
Los Angeles, California 90071

For the Defendants F. M. and R. W. GARRITY and SHAW:

OSWALD & YAP
BY: MICHAEL A. OSWALD (NOT PRESENT)
5000 Birch Street
Suite 4600
Newport Beach, California 92660

For the Defendants LUGO, MANSELL and CIPPARONE:

STEIN & KAHAN
STANTON L. STEIN (NOT PRESENT)
1299 Ocean Avenue
4th Floor
Santa Monica, California 90401

For the Defendant HOLMES:

BUCHALTER, NEMER, FIELDS & YOUNGER
BY: JACK I. SAMET and JOVINA HARGIS

700 South Flower Street
Suite 700
Los Angeles, California 90017

[p. 7] LOS ANGELES, CALIFORNIA; MONDAY, OCTOBER 24, 1988; 1:30 PM

THE CLERK: Item number 17, CV-83-4742-AWT: SIPC, et al. versus Seymour Vigman, et al, consolidated with CV-83-5674.

THE COURT: I am not going to have anybody enter their appearance. If you want to be shown on the minutes as having appeared, you can leave you name with the clerk; and as far as I am concerned, the only people who are here on the argument are just the people who made the motion or opposed them; and then on that basis, first, the plaintiffs filed something called a surreply or attempted to file something called a surreply to the Holmes' reply, and since it's really just a matter of arguing the evidenciary rulings, I am going to ask the clerk to have this filed.

I haven't done it as I customarily do on the morning calendar, indicated a tentative ruling but I will do so now, and this is not addressing the motion to continue the pretrial conference. This is just on the motion for summary judgment. Let's see.

Defendant Holmes has filed a three-part motion, or three separate motions for summary judgment on the causation, on standing, and on the RICO claim.

As I understand it, the first two motions are directed against all plaintiffs, except the class [p. 8] plaintiffs; and the last motion, the RICO motion, is directed to everybody; is that right?

MR. GRAHAM: Robert Graham on behalf of the trustees.

The standing motions as to the securities claims is directed solely –

THE COURT: Excuse me. SIPC?

MR. GRAHAM: SIPC.

THE COURT: I agree with that. All right.

In other words, there is a joinder in this motion by – I forgot. I will call it the Holmes Corporation, for lack of a better word, although I don't mean to draw any legal conclusions from that.

MR. SAMET: It's called Aero Systems.

THE COURT: By Aero Systems.

Here's my view of the Aero Systems joinder: One, I am not going to hear any separate argument on that. But I am going to treat it this way: As far as the objection of the plaintiff is concerned, plaintiff may be correct: In certain respects, it may have argued the motion differently if the joinder has been timely, but I don't think it makes any difference because I am going to limit any affect of this motion on Aero as follows: To the extent any matter is deemed to be established without controversy, I believe it applies to Aero as well; but I [p. 9] don't think a separate judgment can be entered in any event in Aero's favor because even assuming Holmes is correct all the way down the line, my understanding is that the plaintiff's case against Aero is also predicated on activities of Diamond so it wouldn't remove the claim anyway; so there would be no judgment on any claim.

That's how I am going to approach the joinder.

Now, this is my feeling on the motions of Holmes. I believe on the RICO claims – to me that's the easiest one. On the RICO claims, I believe that there are issues of fact raised so that I indicated a probable denial there.

But on the remaining claims, I think my inclination is to grant the motion. I don't known if I can express myself any further. I think the causation claims, it's not so much whether or not there is an issue of fact. It's a question of, I think, attenuation and how far out can you spin the web and still find causation. I think that's almost what it amounts to.

Standing is almost the same thing, except on standing, it appears to me that SIPC has not now shown, as it's required under the Ninth Circuit ruling in this case, that there was some, I don't know what to call it, some wrongful use of the stock.

The only showing is that stock was [p. 10] pledged. It doesn't show if it was wrongful. There is no showing on that.

I think under Celotex now, since that is almost an element of the claim, that at this stage, SIPC has the burden of coming forward with some evidence to support that element of the claim.

So that's sort of the tentative ruling. I think since the matter is largely – well, if it goes into – well, I will hear from Holmes.

Let me put it this way: Just if you want to be heard on the RICO; and then since the tentative ruling is in your

favor, otherwise, then we will get the opposition and give you a chance to reply. How is that?

You want to be heard on the RICO claim?

Mr. SAMET: Just very briefly.

Should I speak from the podium?

THE COURT: I think you should so that the reporter can hear you better.

MR. SAMET: Yes, your Honor.

I think that the same principles which were raised in the causation and standing motions have an impact on the RICO motion and indeed a controlling impact in that if there is no causal connection between the conduct of the Holmes and the demise of the brokerage firm, then the causation element of RICO is missing. I must –

[p. 11] THE COURT: You say – all right. The same causation analysis applies to the RICO claim as it does to the other claim?

MR. SAMET: Right.

THE COURT: Although the analysis is really in terms of, we'll say, security type causation?

MR. SAMET: Yes. Except that if there is no – in effect, if there is no securities claim – the gist of all the claims is if there is no security claims under 10b-5, it seems to me that is also a RICO deficiency and the same applies to standing.

THE COURT: You mean saying that in the sense that there is no predicate act?

MR. SAMET: No, I am not saying there is no predicate act. I am not going to contest Your Honor's ruling that there are issues of fact here.

I am saying the predicate acts are not predicate to the damages. There is no causal connection between what are called predicate acts or acts of racketeering if there are any and the actual damage, the demise of the brokerage firm; and I think the point of causation if it has validity, and I believe it does, has validity not only in the causation motion but the RICO motion as well, and the same for standing and that is even if Your Honor is correct and there could be issues of fact [p. 12] whether there were predicate acts but they are not causely connected and the same for standing.

THE COURT: All right. Thank you.

Who's going to be first up here?

MR. TAYLOR: Can I address the standing and causation issues with respect to RICO, Your Honor?

THE COURT: Yes.

MR. TAYLOR: Stephen C. Taylor of Sheppard, Mullin, Richter & Hampton on behalf of SIPC.

Your Honor, I thought that this might be the issue that the Court wanted to hear. I agree with the Court's tentative ruling.

There is a difference, contrary to what Mr. Samet says, between the standing issues and the causation issues under 10b-5 as opposed to those causation and standing issues under the RICO statute.

The defendants claim that SIPC has to be a purchaser or seller under rule 10B to assert claims under RICO. That's just what he said. That's wrong. I want to point out the case that we have cited in our brief, which is Warner versus Alexander Graham of the 11th Circuit.

There was no such requirement in that case and there was no such requirement for good reason. In Warner there was alleged that defendant Graham had issued a series of false and misleading statements concerning the financial [p. 13] statements of the firm called ESM Broker and the Defendant Graham had participated and abetted in the conspiracy to defraud it.

None of the damages claimed were in connection with the sale or purchase of securities by Warner. Nevertheless, the court flatly stated that the RICO statute has no such court imposed limitation and held that he could state a cause under RICO for damages that he incurred as a result of sales and purchases by others which had the effect of injuring.

Defendants urge the Court to follow the more reasoned view of the Zepkin case in the 4th Circuit.

The Court should not for several reasons. First, Zepkin is easily distinguishable from Warner. Zepkin facts, unlike Warner, involve a matter which really constituted a breach of nothing more than a breach of fiduciary duty. Pure and simple. Never should have been a RICO case in the first place.

The gravamen in Zepkin, unlike Warner where the plaintiffs losses could relate to the sales of securities by others than the Plaintiffs, was merely that plaintiff was

induced to rely upon representation, made advances under those representations.

In Zepkin – Zepkin with these facts, then proceeds to discuss whether or not Congress intended the [p. 14] purchaser-seller restriction to be applied, quote, to a RICO claim based on a 10b-5 violation, end quote.

It first uses the Bernbaum rule as justification for its holding. In other words, it examines the restrictive interpretation of the courts which granted the right of a private party to bring an action under the legislation as to rule 10b which did not grant that right initially, then with reason extends far beyond what the case required, superimposes that restriction over an explicit right granted by congress by its use of the phrase in the RICO statute, "Fraud in the sale of securities."

That's in quotes.

It's just an urge that I quote, "Fraud in the sale of securities," end quote, was not so restricted by congress because it meant the phrase should not be restricted.

The Zepkin court correctly states that congress did not write RICO in a vacuum and indeed it didn't; but yet the Court states that since the vacuum was filled with, quote, hundreds of cases since Bernbaum which followed the Court imposed restrictions on Bernbaum up through Blue Chip Stamp, congress must have meant, quote, fraud under rule 10b-5 when it said, quote, "Fraud in the sale of securities," end quote.

The court says then, quote, "If the Court had [p. 15] intended the drastic result of overturning this consensus, it surely would have done so in a more explicit way."

This to me is tortured logic.

If with all the litigation involving standing under a right explicitly given by congress and when congress explicitly giving a right under RICO, it's much more logical to say that the congress would have said that RICO provided that right by stating that the right existed, quote: For fraud in the sale of securities under 15 USC section 78 JB and rule 10b-5 thereunder. It didn't do that. It used the word "fraud" in the sale of securities.

Now, the Zepkin court states that congress merely intended to expand the range of remedies rather than overturn the settled law.

Well, first, congress overturns law all the time. But in this case when congress clearly expanded the gamut of devices to combat organized crime and which SEDEMA said was to be broadly construed to effectuate its remedial purpose, is it not just as logical to state that the remedial purpose is to stop the kinds of mass fraudulent manipulation cases as in the case at hand.

And can it be interpreted to exclude a party, a private party such as SIPC who have no federal remedy to collect its losses, if congress and the Supreme Court's broad interpretation of RICO is not effected here.

[p. 16] The Zepkin court also asserts the parade of horrors of "what if's" and cites the dangers and vexatiousness of securities litigation as a result by not allowing an action under RICO unless the plaintiff is, quote, a buyer or seller of securities under rule 10b-5.

With due respect to the Court, this is not an excuse to reimpose a court developed restriction on expressed congressional language. We do not have a case here for which the courts need protection.

We are not, as the Court assumes, a plaintiff to be in the absence of the doctrine a, quote, bystander to the securities marketing process awaiting developments on the side lines without risk, end quote.

Rather, SIPC is a private party funded by public members required by law to pay such losses caused by the acts such as those as defendants did herein. There is no danger here as set forth by the Zepkin court.

The examples the court sites relate to causation, not to standing and courts did not ignore the expressed and unfettered language used by congress and take away plaintiff's rights granted by that language.

Indeed, the Ninth Circuit in First Pacific Bank Corp versus Bro, stated there must be, quote, a fraud in the stale of securities, end quote, to proceed under RICO. But the decision does not require that the Plaintiff be a [p. 17] purchaser or a seller.

Had the Ninth Circuit believed as Zepkin rather than Warner, why didn't they simply say that the first Pacific Bank Corp plaintiff wasn't a purchaser or seller under 10b-5. They didn't do that.

They accepted congress' language as it was; i.e., there was not a sale of securities involved in the case.

Further, the Supreme Court is cautioning against this embellishing the language of the statute.

In U.S. versus Lock, 105 Supreme Court 1785, at page 1793 – it's a 1985 case – the Court stated: Nor is the judiciary a license to attempt to soften the clear import of congress' chosen words, whatever the courts beleive [sic] those words to be, would lead to a harsh result," with citations.

On the contrary, deference to the supremacy of the legislature as well as recognition that congress can typically vote on the language of a bill generally require us to assume that, quote, legislative purpose is expressed by the ordinary meaning of the words used, end quote, with citations.

Quote, going down the plain language of the statute in search of a possibly contrary congressional intent is a, quote, step to be taken cautionally, end [p. 18] quote, even under the best of circumstances. Again quotations, or citations, rather.

Finally, we respectfully, your Honor, urge the Court to consider the congressional history of RICO and the Supreme Court's liberal analysis of it.

One of the threats to society that is posed by organized crime in securities matters was specifically considered and was large scale market manipulations when RICO was passed; thus, this is the kind of case that congress had in mind when adopting the language: Fraud in the sale of securities; and contrary to what the Zepkin court said, the United States Supreme Court stated in SEDEMA that, quote, RICO was an aggressive initiative to supplement, and I underline the word supplement, old remedies and develop new methods for fighting crime. That's 473 U.S. 498

Further, it said, quote, that all of RICO's provisions should be read and observed on all the legislative statements about the novel, and I underline novel, remedies at attacking crime on all fronts.

What fraud in the sale of securities here? They include, but they certainly are not limited to, Holmes massive campaign of misrepresentations regarding the CD 3,000 which provided the bankroll for the Bunnington and other manipulations.

[p. 19] Outsider – insiders like Holmes, Vigman and Diamond selling Aero Systems stock at inflated prices, all sales in furtherance of their scheme and all sales profiting them individually.

Insider trading by Holmes, Vigman, Diamond, Blumenthal and others especially the sale of Aero Systems stock by Vigman and the culmination of the 1976 plot of selling those securities to Mr. Lugo so that he could continue to maintain the Bunnington manipulations and the Aerosonics manipulations; Holmes' purchases and sales of Bunnington stock to falsely reflect market activity in Bunnington; preferential treatment to Mr. Holmes by Mr. Lugo. Mr. Holmes' parking. It was a sale and recorded as a sale and shown by Mr. Holmes on his own documents as a sale conveying legal title to hide beneficial title.

Holmes sale in 19 – in November of 1980 of inflated Aero Systems stock to buy Bunnington stock, a classic 1962a violation.

Holmes publication of false Bunnington press releases to aid in the Bunnington manipulation.

Holmes publication of false information concerning Aerosonics, the so-called collision avoidance device.

Holmes participation in the stock manipulation by creating a sham dealership for Cascade Data. It could [p. 20] go on.

In sum, the Zepkin court formulated another restrictive impediment to RICO in a case which was not a case in which RICO should have been argued at all. It did so in light of the clear admonition of the Supreme Court in SEDEMA that RICO is to be read broadly and used broadly to provide new remedies and that is I respectfully urge, Your Honor, as far as standing is concerned the court has every right to follow the dictates in the Warner case and the concepts set forth in Zepkin.

That applies to standing and Mr. Samet briefly addressed the causation issue and you want me to address that.

It's slightly different.

THE COURT: You mean causation in the RICO context?

MR. TAYLOR: Yes. In the RICO context, this business about lost transaction and that kind of thing.

THE COURT: Go ahead.

MR. TAYLOR: Holmes' causation argument rests on the legal argument: Plaintiff's can't show causation. In other words, the legal link between plaintiff's damages and Holmes acts, whether you call it loss causation or flow or indirect injury or intervening cause or too remote, whatever label you put on it, it boils down to whether or

[p. 21] not there is a sufficient nexus between those acts and the damage caused to us.

Holmes seems to concede, as well he should, that the Aero Systems manipulation by itself is a question of fact for the jury.

And this causation argument seems to be hinged on two factual contingents; first, as shown on page 12 of his opening brief, Holmes claims that if a manipulation of Aero Systems stock had caused the brokerage firms to fail, one would expect to see large quantities of Aero Systems stock in the inventory and that the Aero Systems stock price would fall precipitously.

Rather, they say: This is based on a hearsay exhibit with no foundation, an ASD report. They say that Bunnington stock was held in large quantities in the inventories and its stock dropped precipitously on the collapse of the brokerage houses.

In short, Mr. Holmes is saying: I didn't cause it. The Bunnington manipulation caused it. It's an important fact to remember in their argument, Your Honor.

Second, Holmes states on page 45 of his opening brief that it was the decision of Lugo and the Sebag brokers that were the direct and intervening cause of the collapse, end quote.

[p. 22] Holmes implies that plaintiffs rely solely on Mr. Holmes' manipulation at Aero Systems stock to connect him to the collapse and this is simply not the case.

For the sake of argument, let's accept the fact that Holmes' arguments are correct; in other words, Bunnington caused the collapse and Lugo's independent acts of accumulating inventory caused the collapse.

If you accept those two arguments, Your Honor, Mr. Holmes is condemned himself to a trial by jury. Holmes' culpability for the loss can be adjudged by a jury without even mentioning the Aero Systems manipulation.

First, there is a mountain of evidence to go to the jury about Holmes' conspiracy with Mr. Vigman and Mr. Lugo; and if the Court believes that it's a jury question regarding whether or not Lugo and/or Vigman manipulated Bunnington stock or whether or not as Mr. Holmes' asserts Lugo was the one that bought up all the Bunnington stock, then Holmes, as a conspirator or aider and abettor or whatever you want to call him or both, is just as responsible for those acts as Mr. Lugo and/or Mr. Vigman.

If the decisions of Lugo are indeed the direct cause of our damages, Holmes says on page 45 of his opening brief, then Mr. Holmes is Mr. Lugo's baggage.

Let's look at the flow of the cause from the Bunnington stock manipulation which Holmes, at least in his [p. 23] motion concedes, was the cause of the collapse and let's put Mr. Holmes in that flow.

The history of the Holmes' relationship with the principals of Bunnington, the felon Vigman and under indictment Mr. Joe Lugo, go back to 1967 as set forth in the statement of facts.

The first time that we can locate that Mr. Holmes owned stock in Bunnington was the same year that it was incorporated in 1969, 20,000 shares.

In September of 1979, Mr. Holmes bought a Bunnington convertible debenture for $100,000, convertible into 40,000 shares of Bunnington stock.

Now, Your Honor, I am going through this whole thing without mentioning the Aero Systems manipulation.

Now, this debenture is an important factor because it should be for a jury to decide whether or not this served as a motive. This debenture served as motive for Mr. Holmes to do what he did regarding Bunnington.

The stock he obtained there was convertible upon the conversion payable at $2.50 a share would have been worth 10 to $12 in September of 1981, less than two months after the collapse had Mr. Holmes and Mr. Lugo and Mr. Vigman not caused the collapse of First State and Sebag. But this, Your Honor, again should be for a jury to decide whether indeed it's a motive.

[p. 24] At or about the time Mr. Holmes purchased this debenture, he started purchasing blocks of Bunnington stock, and I have a copy of an exhibit I'd like to show you. It's in the record prepared by Mr. Holmes himself.

Counsel will know what it is since I had to fight to get it from him. If I could hand that up.

I have highlighted on all copies. It's Exhibit 3863 for identification. This is produced during Mr. Holmes' deposition, Your Honor.

If you will note on the second page, I have highlighted transactions which show a very interesting pattern. I don't hesitate using that word in this case because it fits right in the pattern.

You will note there are successive purchases, which are blue lined by Mr. Holmes, through First State Securities of Bunnington stock.

Six, I believe, purchases of 5,000 shares each, one purchase of 2,500 and they are spaced fairly regularly. Then after each purchase, there are a series of sales through other brokers, small sales: A thousand here, 750, 500, 600, 200, definite pattern.

Our expert has concluded, and it's for a jury to decide, whether or not indeed this was Mr. Holmes direct participation in a manipulation.

Your Honor, during this period of time, Mr. [p. 25] Holmes and Mr. Lugo dominated the market in Bunnington. That's Mr. Holmes and Mr. Lugo dominated the market of Bunnington.

On these days, there were some days when his purchases and his sales were 90 percent of the volume of that stock.

The pattern itself suggests to me, a layman, not a stockbroker, that Mr. Homes is buying blocks and selling out to create a market and indeed our expert has said so. But in any event, regardless of what I think and regardless of what our expert thinks, I know that Mr. Samet thinks differently; but, really, it's for a jury to decide

whether Mr. Homes was directly involved in the manipulation of Bunnington stock, the very stock, the value of which according to Mr. Holmes caused the collapse.

This is further interesting, Your Honor, this one exhibit, because as you can see, there is a red line across one transaction. That transaction, Your Honor, was a parking transaction. It's the only instance out of all these trades, all of them, where Mr. Holmes sold stock, so-called sold in quotes, through Joe Lugo's firm. Why is that?

Well, the jury will decide it, but we'll urge the jury to the view that it was because it was a part that it was the only so-called sale through Joe Lugo. It [p. 26] disrupts the pattern.

And you will also note one other thing about this exhibit, Your Honor, the graphic growth of price of the stock between the 30 entry – excuse me – August 17, 1979, 350 through 5/5/81, 11.37, down to 5.29; the day of the park, $12. Quite a growth.

Getting to the park, Your Honor, the parking transaction, Mr. Holmes cries that it was not park. Again, this is a jury question to decide. The plaintiff's expert says that it was. And it's interesting to note that the expert says and the evidence shows that Mr. Holmes, because of the nature of the transaction, knew that it was a park.

Again, he didn't think about his motive to back this debenture. He sees Bunnington stock needs help. Joe Lugo comes to him, asked him for the first time in history of the firm, "I have got to have a sales transaction. I have

got to have you buy stock from me to get it out of my inventory."

It shows intent, Your Honor. It shows an absolute direct involvement by Mr. Holmes in maintaining price of that stock, of protecting the price of that stock, of knowing that Mr. Lugo is in trouble and needs to buy this stock and have it inventoried; at least he needs to keep the price up. It shows a direct, knowing intent and direct implication of Mr. Holmes.

The expert, our expert says that Holmes and Lugo jointly dominated and controlled the Bunnington market.

But I think the Court should descide [sic] whether or not it's a park and whether or not Mr. Holmes intentionally participated in the Bunnington manipulation.

Again, this is all seen in the context. It should be seen in the context of Holmes' motives. He had two motives, Your Honor, that I think the jury should decide: One is to protect his friend Mr. Vigman who was a major shareholder in Bunnington and to protect his friend Mr. Diamond who was a major shareholder in Bunnington.

Two, he wanted to protect the inflated price of Bunnington because he wanted to protect his investment in that letter, that convertible debenture rather.

He only needed to do it until September when, through the inflated price, through manipulation, he could sell his shares under rule 144. He missed it by two months.

Also, Your Honor, this is the only place in the Bunnington manipulation where I have to mention the Aero Systems manipulation, but Mr. Holmes expedited Mr.

Vigman's 144 sale so that Mr. Vigman could get money into Lugo to perpetuate the Bunnington and Aerosonic acquisition.

Now, in addition, Holmes promoted Bunnington [p. 28] stock through Moore and Schley. He introduced Moore and Schley to Bunnington principals who sold their Bunnington stock through Moore and Schley.

Holmes sent Moore and Schley a Bunnington press release with false and misleading statements in it.

Holmes discussed with people from Moore and Schley the availability of financing for Bunnington. Holmes profitted [sic] from insider information with respect to Bunnington; and saying all this, I am avoiding all of the prior relationships between Mr. Holmes and Mr. Vigman and Mr. Lugo which are all set forth in the statement of facts.

Now, if it isn't a jury question as to whether or not Holmes directly participated and, in fact, materially assisted in the Bunnington manipulation, isnt' a question of fact.

When Mr. Holmes' own argument says that Bunnington caused the collapse of First State and Sebag, that is the direct flow; and in that scenario, he's no assistance from the obvious Aero Systems manipulation of Holmes, Vigman and Lugo. It is on its own and by Holmes own argument a scenario which must let a jury decide whether or not Holmes is directly responsible for the collapse.

Now, unless Holmes tries to argue that Lugo did it all, is it not for the jury to consider the same [p. 29]

factors: Motive, trading patterns, domination of the Bunnington market by Holmes and Lugo, preferential treatment given Holmes by Lugo, Holmes' knowledge of the participation in the parking transaction with Lugo, the prior relationship between Holmes and his friend Joey Lugo and the fact that Lugo got insider information concerning Aero Systems from Holmes, and shouldn't the jury be able to decide from those and other facts whether or not Holmes was indeed with Lugo and is indeed responsible for Lugo's acts of accumulating Bunnington stock and falsifying documents to try to help the Bunnington manipulation and keep it going and protect Mr. Holmes' debenture.

Thus, by his own arguments, Holmes in furtherance of the Bunnington manipulations has put himself directly into the collapse of those brokerage houses and a jury should decide first whether or not he did it.

I believe the jury would decide that; but, secondly, Mr. Holmes' liability for them.

Now, with respect to the Aero Systems manipulation, Your Honor, that's the second portion I wanted to address.

I don't believe that even Mr. Holmes' counsel would say it's not a jury question to say whether or not there was a manipulation, or whether or not Mr. Holmes participated in it or whether or not Mr. Lugo and Mr. [p. 30] Vigman participated in that.

Their argument is remoteness. I contend, Your Honor, that even the Aero Systems manipulation itself is not too remote. In the first defendant, Holmes, in his papers, has

attempted to dissect and insulate various elements of his fraud.

To allow this and to hold that various isolated incidents cannot go to a jury moors the lines of the cases such as Kaplan and Competitive Associates which we cited in our papers which hold that so-called loss causation, which is a term, I think, an artful term which really has no meaning beyond causation itself, cannot be judged on separate misrepresentations but on the effect of the entire scheme or artifice to defraud.

Indeed, it's this concept which most fully applies SEDEMA's caution that RICO must be read and applied liberally.

It's the entire scheme that hurt the plaintiffs, not a single representation by Holmes or act by Vigman or act by Lugo.

THE COURT: You are still addressing the RICO causation?

MR. TAYLOR: I am still addressing the RICO cause of action and the first part of my presentation which goes solely to holding Mr. Holmes in on the Bunnington [p. 31] manipulation alone, the one he says caused the collapse. Okay. Let's accept that.

Then the jury should decide whether or not he's part of it and I think we have more than sufficient facts to go to the jury on that issue.

THE COURT: What about causation in the securities act?

MR. TAYLOR: Causation in the securities?

THE COURT: Yes.

MR. TAYLOR: The causation – the causation in the securities area is handled by fraud in the sale of securities, Your Honor. It is much broader than your traditional 10b-5 causation scheme.

As I pointed out, in our case of Warner, the Warner case, let me point out that Holmes is saying "Hey, you can't hold me liable for the Aero Systems manipulation because, gee whiz, the Aero Systems manipulation didn't cause the collapse. It was too remote." That's what he says.

First he's saying that the Bunnington manipulation did it and I say, "Okay. Let's accept that." And now I am showing how the Aero Systems manipulation was really part of a scheme and as such is not remote at all because of a case which I will cite to you.

It's the entire scheme which hurt the [p.32] plaintiffs, not by a single representation by either Holmes or Lugo.

As we can see in the Bunnington manipulation, it was not just false press releases and SEC filings, but Lugo and Holmes' domination of the market, Holmes' pattern of buying and selling and his parking is attributed to him.

They cannot be isolated as the Aero Systems manipulation should not be isolated to the entire scheme and to effectuate what RICO is supposed to do.

If ever, Your Honor, there was case to apply RICO and to let the case go to a jury, this case is it.

Let me show you how – and it's our argument that because of this, as shown in the causation brief, the Aero Systems manipulation – can you put those cards up, please.

I want to illustrate just graphically the Aero Systems price rise in connection with the statements made in the press and on a time line together with the sales made by the principals.

This document duplicates what is the – it's nothing new – duplicates what is attached to the expert's declaration, Your Honor. So it's not a new exhibit. The defendants have seen it. The only thing that's different is that it's colored red to show the activity.

The stock price on the left and the date at the [p. 33] bottom as the exhibit and the dates of various publications of the articles which we contend were misrepresentations together with the amounts sold by all of the principals, or some of the principals: Mr. Vigman, Mr. Holmes, Mr. Spire who is Mr. Vigman's son-in-law, Mr. Blumenthal.

You can see the concentration in 1981 on the right. See how it starts going up and keeps going up and it's maintained? It's rather graphic. It's not only graphic, but our expert says that it's absolute evidence of the manipulation.

Now, it's this manipulation that defendant says causes no damage.

Your Honor, we are entitled to prove all elements of a scheme and this is a vital element of that scheme.

The scheme was conceived in 1976 when Vigman and Diamond got valuable Aero Systems stock for worthless DCS stock, and I am sure at that time that the exact nature of how the stock would be sold or what gimmick would be gotten to sell it was not apparent, but there was no matter because Vigman had to wait and Mr. Holmes had to – sorry – vigman [sic] had to wait at least two years under rule 144 before he could sell his stock anyway.

Well, when the CD 3,000 thing came along, it was just the right thing for the conspirators. They [p. 34] accused me of using the word gimmick in connection with it in the brief, but I didn't choose the appellation. That was chosen by an ex-officer of the Aero Systems that called it a gimmick.

Now, Holmes profit early is shown on the chart under the scheme. Vigman profitted [sic] along the way and the manipulation of Aero Systems continued into the early spring of 1981, into the summer.

Now, it's clear from the facts and according to our expert, it's indeed a fact that Vigman, who was assisted by Holmes who expedited Mr. Vigman's release of the Aero Systems shares under rule 144 became Lugo's bankroll to continue the manipulation of Bunnington and Aerosonics which benefitted [sic] both Vigman and Holmes' interest in keeping the Bunnington price stock up particularly.

Now, Holmes denies this but it's the province of the jury to decide whether or not the Aero Systems manipulation was a device used by the conspirators not only to

line their own pockets but to keep the price of Bunnington going up or stabilizing, the very Bunnington manipulation which Mr. Holmes contends was the reason for the collapse.

Thus, the issue is not as defendant would, Defendant Holmes, would have the Court believe. It's not [p. 35] whether or not there is a loss causation or an intervening cause or some other purported legal impediment attached to the Aero Systems manipulation alone, but rather was the Aero Systems manipulation part of a scheme, part of a scheme not only to manipulate Aero Systems but part of the very scheme that they contend caused the damage of the Bunnington manipulation, and it was. Our expert says that it was.

And you may not believe it and Ms. Keir may not believe it and the audience may not believe it and Mr. Samet may not believe it, but a jury might and that's why it's a jury question.

Now, they cite certain cases. They are inapplicable.

First, I'd like to cite to the Court a case that I found on Saturday called Bastian versus Petron Resources Corporation. It's 681 F. Supp. 530. I am sorry I didn't cite it in our brief. I simply didn't find it. Northern District Illinois, 1988 at page 537.

The Court found no pattern but regarding loss causation, it says, and I'd like to quote: Defendants have moved to dismiss on three grounds. First, against the insufficiency of 10b and the 1780 claims means that the defendants have failed to sufficiently plead in predicate acts of racketeering activity; and, third, the third ground

[p. 36] was they alleged a RICO violation and they lack standing because they don't allege how they were injured by it.

The Court then says: The first and third elements, that's the standing and the third element, indicates that the defendants misconstrue the interaction of the securities laws and RICO claims predicated on them.

As defendants themselves argue, plaintiffs fail to state a claim under counts one and two not because defendants have not violated the securities laws, but rather because courts in implying private rights of action under these laws have imposed an additional, quote, loss causation requirement end quote.

Then it cites Newman saying, "It is only because the judiciary has created a private cause of action for damages under 10b, the contours of which are not described in the statute, that standing in such cases has become a pivotal issue," unquote.

Now, the Court goes on to say after quoting Newman, "This judicially imposed limitation on such right of action simply does not apply to the statutorily created RICO claims.

THE COURT: I thought we were switching over to the securities?

MR. TAYLOR: That's what this is. This is under RICO. We are not switching back to the security [p. 37] action.

THE COURT: I thought we were going to go over into the securities?

MR. TAYLOR: Oh, no.

THE COURT: I'm not interested in hearing anyting [sic] more about RICO.

I asked you to talk about the standing under the Securities Act.

MR. TAYLOR: No, what Mr. Samet was saying was, "Gee, since they don't have any standing –

THE COURT: I know what he was saying. I am asking you now to address the other parts of the tentative ruling. I thought I did that about five minutes ago.

MR. TAYLOR: Oh, no. I am done if that's the case. I am only addressing RICO and saying that the ruling is correct.

THE COURT: You are conceding that there is no standing under the Securities Act?

MR. TAYLOR: I am conceding that – I can't concede that.

THE COURT: Well, I said, you are not interested in arguing further?

MR. TAYLOR: All I am saying is that as far as the argument that Mr. Samet made, that you should apply the same standard –

[p. 38] MR. GRAHAM: Your Honor, I am going to address the elements.

THE COURT: All right. Take your turn.

MR. TAYLOR: All right. Thank you.

THE COURT: Just a minute. Before we do, I want to get to this very short, I hope – I have a criminal matter, all right, because I think we'll be here a few minutes longer on this.

I am going to recess this SIPC versus Vigman 10 or 15 minutes or so. All right.

MR. SAMET: May we leave our papers here?

THE COURT: Yes, you may.

(Brief recess had).

THE COURT: We were about to hear from Mr. Graham on what?

MR. GRAHAM: That's correct, your Honor. As to the claims brought by the trustees under section 10b on the issue of causation.

THE COURT: All right.

MR. GRAHAM: Your Honor –

THE COURT: So you are not speaking to the standing issue?

MR. GRAHAM: I am not speaking to the standing issue.

THE COURT: I said issue. I meant the standing [p. 39] motion.

MR. GRHAM [sic]: Let's clarify something, and perhaps there was some confusion. Is it my understanding that as to the standing issue, the court's order or tentative ruling is that the 10b-5 claim of SIPC would be dismissed; is that correct?

THE COURT: That's the only motion that's made.

MR. GRAHAM: I am going to address the 10b claims of the trustees to which a motion for summary judgment has been made based upon causation is that the court's tentative ruling –

THE COURT: Not only against them, but also against SIPC.

MR. GRAHAM: Plus against SIPC, but let me take the trustees.

Is it the tentative ruling of the court that the trustees claim has been dismissed for –

THE COURT: Not has been, but should be.

MR. GRAHAM: – should be dismissed for lack of causation?

THE COURT: Yes.

MR. GRAHAM: Your Honor, let me point out a few things to which Mr. Holmes' concedes. He concedes that his client, Robert Holmes, participated in a manipulation of Aero Systems stock. He also concedes for the purposes of [p. 40] the motion that Bunnington Corporation was among the securities, as well as Aerosonic, that caused the demise of the brokerage firms, Sebag and First State.

There has been ample evidence submitted showing a group of people of Mr. Holmes, Mr. Vigman, Mr. Lugo, Mr. Garrity, working together in a scheme to manipulate these series of what has become known as the target securities, throughout the period of time, at least through 1980 and 1981.

In regards to the court's tentative ruling, the trustees would like to understand the court's problem with the attenuation between the conduct to which Mr. Holmes admits to and the loss.

As we see it, the attenuation is resolved because of the fraudulent scheme that has been set forth clearly in the evidence in which – a scheme to which Mr. Holmes concedes, although he said Mr. Lugo and Mr. Garrity weren't part of it. I mean, that's an issue of fact, so I am a little confused there, so if the Court has a specific inquiry regarding the trustees' claim under 10b, I would invite – I invite that inquiry.

THE COURT: Well, let me do this. You think your position is different from SIPC on causation?

MR. GRAHAM: On the causation, there is some distinction, yes.

[p. 41] THE COURT: Tell me what you think the difference is?

MR. GRAHAM: The distinction between SIPC and the trustees is that the trustees held in their inventory, in their inventory, large amounts of Bunnington stock, large amounts of Aerosonic's stock. It's the trustees position that because of the fraudulent scheme, that Bunnington and Aerosonic stock ended up in their inventories.

We submit that the evidence showing the scheme involving Mr. Holmes, Vigman, Lugo, Garrity, over a long period of time manipulated these series of stocks.

It's our contention that this is somewhat like musical chairs. If the music had stopped, so to speak, in January

of 1981 instead of July 1981, the picture would have been different.

The evidence submitted shows that at that time there were excessive inventories of Aero Systems stock and had the music stopped in January of 1981, we would be sitting here arguing about one of the other parties seeking a motion who is a participant in this scheme, a motion for summary judgment.

The point is: All of these securities were manipulated by this group of individuals and it just so happens that the Aero Systems manipulation in essence came [p. 42] to an end. The main participants had cashed out their chips and were then using the proceeds to keep the other stocks in a manipulated condition, keep the manipulation going.

As pointed out very strongly and very clearly by Mr. Taylor, there was clear motive by Mr. Holmes to keep that Bunnington stock going, a motive that caused him to park stock, caused him to promote Bunnington actively. Those are all parts of this fraudulent scheme and the test under section 10b for loss causation where a scheme is alleged is that it's the nexus between all the interacting elements of the scheme and the economic loss.

And that, I think, is what has been lost in all the paper that has been filed is the test of: All the participants of the scheme, their interacting elements, their various conduct taken as a whole and the economic loss.

THE COURT: What is, for instance, the loss to the trustees from the parking transaction. All that meant was, it seems to me in the end, the life of, we'll say, FFSC was extended a little while longer.

What's the loss?

MR. GRAHAM: The loss, one, for FFSC extended the life and brought down Sebag because the evidence shows of the large purchases taken into Sebag during that period [p. 43] of time from the end of May through July.

Now, the impact at First States is significant by the larger economic loss that's been suffered from the end of May to when the firm went out of business in July; in an area-hood of half a million dollars, did the loss increase.

Now, there is much made in the motions about the net capital deficiency as Mr. Holmes claims that the net cap deficiency was not caused by Mr. Holmes but the test is not the net capital deficiency issue. It's the economic loss: Did the conduct of the scheme cause the economic loss?

The participants in this scheme all share that responsibility. Mr. Holmes specifically shares that responsibility in relationship to FFSC through the extension of the life of FFSC and causing an economic loss of half a million dollars more than had the business ceased to exist in May of 1981..

THE COURT: All right. Anything else?

MR. GRAHAM: In conclusion, Your Honor, there is the attenuation problem.

When one examines the fraudulent scheme concept and the evidence which has been presented, there is ample evidence for this court to conclude that this issue should go to the jury.

[p. 44] MR. BONNER: Your Honor, Joel Bonner for SIPC. I can address, if you would like, the standing issue as it relates to the motion brought solely in SIPC.

THE COURT: Under the Securities Act?

MR. BONNER: That's right.

In your tentative ruling, Your Honor stated that SIPC, in your opinion, should come forward with evidence of a wrongful use of the stock that was pledged.

THE COURT: Well, what I mean to say is: There is no evidence either way whether or not the pledge was authorized; right?

MR. BONNER: Yes, there is evidence of that, Your Honor.

THE COURT: What is the evidence?

MR. BONNER: There is a declaration filed by Mr. Stranahan who was the SIPC representative in charge of the liquidation of First State.

THE COURT: But he doesn't know whether it was authorized or not.

MR. BONNER: He doesn't know whether the pledges were authorized or not?

THE COURT: Yes.

MR. BONNER: I believe he does, Your Honor. They were able to determine which of the stocks were fully paid for customer stocks and which were not.

THE COURT: All right. So what?

MR. BONNER: The fully paid for customer stocks were stocks that could not be pledged under the law under the SIPC regulations.

THE COURT: I don't think that's accurate. That's the whole point. You are just relying on what you perceive to be a legal presumption, and I don't agree with that. I don't think it's quite black and white.

I don't believe there is an absolute prohibition; and even if there is a prohibition, suppose the customer authorized it anyway? There is no proof that the customer didn't authorize it, is there?

MR. BONNER: Your Honor, I think that the proof is two-fold: One is that it's illegal and –

THE COURT: That's not proof. That's statement of a proposition of law.

MR. BONNER: Okay. Secondly –

THE COURT: And a point with which I disagree.

Go ahead.

MR. BONNER: Okay. Let me point out that assuming that it's illegal and let me cite to you 17 CFR 240.8c-1 and 15c-2-1.

Assuming that it would be illegal for a broker to pledge fully paid for customer stock, why would a customer in his right mind authorize the broker to pledge [p. 46] that stock, his own stock?

THE COURT: Was there some secret promise for a higher return? I have no idea and neither do you.

MR. BONNER: Your Honor, at the very least, the defendants have not come forward with evidence that any of this stock –

THE COURT: It's not their burden. It's your burden under Celotex to prove every element of your claim, that's one of the elements that you have standing and the Ninth Circuit said so in so many words. You took the appeal from the motion to dismiss and the Ninth Circuit says, "Well, you haven't shown us any way that you can state a claim, but you claim you can, so we'll give you a shot." And you have had your shot and you haven't shown it.

I mean, your case is based on speculation. There is no proof at all that the customers didn't authorize it. There is not one shred of evidence, admissible evidence, to support that theory.

I agree it's a plausible theory.

MR. BONNER: And, in effect, that's what we are saying, that it is implausible to think that of the thousands of shares –

THE COURT: But you can't go to the jury with that.

MR. BONNER: – of customer paid stock, that [p. 47] all of those shares were authorized by customer to be illegally pledged.

THE COURT: But you can't go to the jury on the basis of plausible evidence. You have to have some proof.

I think if that's what the evidence consisted of trial, I would grant a directed verdict because there is no evidence to support your claim.

MR. BONNER: I don't think I have anything further.

THE COURT: All right.

MR. BONNER: Your Honor, if I may be heard on just one point that I failed to address when you asked was there anything more.

I would like to emphasize, again as has been made a number of times, going all the way back to the first motions made, that the trustees stand before the Court with a 10b claim in the same shoes as any other purchaser or sellers of securities.

I wanted to reemphasize that we are not just a member of the class and we ended up owning stock at the end and we are damaged by that.

And in that situation, we are not any different than anyone else who purchases securities.

THE COURT: All right.

Mr. Samet, you want to be heard further?

[p. 48] MR. SAMET: Just really very briefly, Your Honor.

Much time has been taken up and I will be less than two minutes, I believe.

First, on the question of whether the trustee is or isn't like SIPC, I think they are in the identical position. The trustee said the only difference is that the trustee held Bunnington stock in its inventory and somehow that makes the trustee a purchaser.

I don't see that as a difference. The trustee didn't purchase the Bunnington stock. They simply held it as trustee and then administered back to the various customers of brokerage firms; so I see the trustee and SIPC in the same shoes. I see no difference between them with regard to the causation issue.

Mr. Graham mentioned that he thinks the parking transaction extended the life of First State. The issue is not "did the parking transaction extend the life of First State"; if the life of First State went on, it could have gotten better. It could have gotten worse.

The point is that whatever happened to First State after the parking transaction and even through the parking transaction wasn't caused by Holmes. It was caused by Lugo and people at First State that did whatever they did.

[p. 49] I wanted to briefly respond to the RICO points. I think the controlling case there is the National Enterprise case that was cited in all the papers which says if effect that an indirect victim cannot sue when they have other remedies, and I think what we have here is SIPC and the trustees are indirect victims of any RICO damage, if there was RICO damage.

You have got a class here and the class is the real party in interest and SIPC and the trustees are almost poaching on their claims, if you will. The class should assert those claims themselves.

With regard to whether or not one needs 10b-5 standing to proceed under RICO, it seems to me that the better view, and I understand the circuits are in disagreement

on this, but it seems to me that since the idea of RICO is that there has to be a real egregious underlying claim before the extreme remedies of RICO come into effect, it seems to me that if a person or an entity doesn't have the standing under 10b-5, they shouldn't be given the greater opportunity to pursue something under RICO if they don't have the underlying claim in the first place.

If there is no standing under 10b-5, the argument is more compelling that there should be no standing under RICO.

[p. 50] That's all I have to say. Thank you.

THE COURT: Mr. Samet, you do agree that the cases differ on it? In other words, there are cases on both sides of that?

MR. SAMET: Yes, I do know the circuits are split on that.

MR. GRAHAM: Your Honor, just one response to Mr. Holmes' counsel remarks.

I think it should be clear that the trustees stepped into the shoes of the two brokerage firms. The trustees stand with 10b claims based upon the fact that they were – that the firms of First State and Sebag were purchaser and seller of securities; not the fact that the trustees, when they took possession of the assets of the firms merely administered the stock that was presented.

MR. SAMET: If I may, Your Honor. That is a different claim than I thought the trustees were pursuing. I thought the trustees were pursuing a claim for the entire estate. If they are pursuing a claim now that's a purchase of only a limited share of inventory of Bunnington or

Aerosonics, that's a different claim than was heretofore asserted.

THE COURT: Can you respond to that? Which claim are you going –

MR. GRAHAM: Yes, Your Honor.

[p. 51] I believe we go back all the way to the motions to dismiss. The basis of the court's ruling in that earlier, almost four years ago, was that the trustees stepped in the shoes of the companies, the two brokerage firms and on that basis were purchasers and sellers of securities. That is what, one, a trustee acquires when he takes over a brokerage firm, all the claims that the trustee – that the company could have brought, the trustee can bring on behalf of the company once it's in liquidation.

THE COURT: If you stepped into the shoes of First State; right?

MR. GRAHAM: That's correct.

THE COURT: I never thought of this now: There is some showing we'll say that First State was in pari delicto; right?

MR. GRAHAM: There is no showing that First State is in pari delicto. There may be an issue, and probably would be an issue raised by the defendants that Mr. Lugo might have been in pari delicto, if by his conduct, but that does not necessarily go to the corporation.

THE COURT: You mean he was acting –

MR. GRAHAM: That is an issue of fact that has to be determined.

[p. 52] THE COURT: He wasn't acting on behalf of the corporation?

MR. GRAHAM: That's correct. If he's participating in a scheme and using the corporation as the device in which to carry out his conduct and leaves the corporation holding the bag for all this Aerosonic and Bunnington stock, then I think pari delicto does not apply as to the corporation.

THE COURT: Anyway, your position is that the trustees succeeded to every claim that might have been asserted by the brokers?

MR. GRAHAM: That's correct, Your Honor. By the brokerage firms.

THE COURT: All right. All right.

Anything else, Mr. Samet?

MR. SAMET: No, Your Honor.

THE COURT: Mr. Taylor, anything else?

MR. TAYLOR: Is there anything else you want to hear in light of Mr. Samet's comments?

He said that there was supposed to be an egregious underlying claim and I submit there is one here.

THE COURT: All right. Thank you. Thank you.

I don't think I changed my mind, but I am not certain. I am going to have to think about the matter again in light of the arguments, but I have to tell you: [p. 53] My inclination is as I indicated earlier, but I am not completely set on it. So I am going to take that under

submission but I am going to rule within the next few days because we have to get on with this case.

MR. SAMET: Thank you.

THE COURT: All right. Now –

MR. TAYLOR: Excuse me. You did get the Bastian cite that I gave you? That's 681 Fed Supp., 530?

THE COURT: Yes. At 537.

MR. TAYLOR: Yes.

THE COURT: We have the motion of, I will call them the Dash defendants, to continue the pretrial. Here is my notion and then you can speak to this.

I think plaintiffs opposed the motion. I think one of the defendants at least joined.

Here's what I think I will do. I think – I frankly don't think that remaining discovery affects pretrial.

As I understand it, that's for expert witness discovery.

MR. MARCUS: That is expert witnesses and there is also concern on the part of the Dash defendants and Martin Blumenthal that in the course of discovery of one expert, he was basing an opinion of fraud on documents which had not been disclosed by the plaintiffs during [p. 54] pretrial discovery and that there would be a motion to either strike that witness's testimony or reopen discovery with respect to this new document.

THE COURT: I can't rule on that motion yet.

MR. MARCUS: I understand that, but that's still pending.

THE COURT: Here's what I intend to do: I intend to hold the pretrial conference, but the only relief that is really needed is to allow, we'll say allow additions to the expert – excuse me – to the witness list and to the exhibit list in light of the discovery that is not complete until a certain time after that and that shouldn't at all affect the preparation for pretrial to any substantial degree. Now that seems to me to be the sensible thing to do now. You can address that.

MR. MARCUS: Yes, Your Honor.

The whole concept of briefing schedules and discovery cutoff and expert schedules was to get to the point that before we had to sit down and figure out what issues were left in this case, the parties would have an opportunity to complete their discovery, complete the discovery of expert witnesses, file their motions for summary judgment and have those heard and resolved before having to sit down and go through the very complex task of preparing a pretrial order in this case.

[p. 55] You can see from just the complexity of this one motion brought by one set of the nine sets of defendants in this case, that one rule 9.4 meeting is not going to be sufficient; that the parties are, until we can complete the discovery that is outstanding, are not in a position to sit down and try to stipulate what issues are in the case, what facts are stipulated, what facts are at issue.

And to rush that process at this point I think in the overall context of the case, a 90 day continuance of the pretrial conference, given all the continuances that have been requested by the plaintiffs of this case, would not be

prejudicial. And it would lend itself to a much more orderly process.

My suggestion would be that the meeting this Wednesday be a preliminary meeting to set up schedules for exchanging of proposed stipulated facts and issues while the remaining discovery and motions be completed; and once that happens, the parties are in a much better position to sit down and make the meetings and the pretrial conference meaningful rather than have these meetings of the pretrial conference where essentially everything is left up in the air.

It's a difficult case to manage. There are a lot of parts and each part itself is very complex; and to [p. 56] rush this thing to a pretrial conference now just doesn't make any sense.

It would be a lot of wasted time on the part of the defense counsel to have each one sit through meetings with eight other defendants where they are not in a position to contribute anything before discovery is completed, before the issues are joined.

The Court has made some rulings today that at least with respect – at least made tentative rulings if they stand at least with respect to the parties that have moved may affect the issues to be tried and other defendants upon completion of discovery are waiting to make their motions as well. And to have a pretrial process with those issues outstanding would seem to be wasteful.

MR. SAMET: Your Honor, I would just like to indicate that I think the Court's course of action that you suggested would be fine. I think essentially the pretrial

schedule can go ahead the way it is with flexibility in view of the size of the case; that there be permitted additions based on discovery of additional experts, additional documents, additional witnesses; and as long as the pretrial is not fixed in concrete, it will move the case along to get most of it done.

My guess is that we could have a 90 percent pretrial in accordance with the existing schedule and do [p. 57] the additional clean up within the next few months following the pretrial.

MS. McDANIEL: Susan McDaniel for defendant Martin Blumenthal.

We join in the Dash defendants motion for continuance of the pretrial in large part because we agree with the Dash defendants that I don't think it's possible to hold a meaningful pretrial conference at this time and particularly to meet with seven or nine sets of defendants where plaintiffs at this time are trying to structure and narrow the issues.

As was noted in the Dash defendants motion, largely because of the illness of plaintiffs major expert, Mr. Seiden, all of this discovery has been pushed over; and not only the discovery, but especially the summary judgment intending to be brought not only by the Dash defendants but also by my defendant. In light of that, Your Honor, those –

THE COURT: Are you saying you have a summary judgment motion that hinges on discovery not yet done?

MS. McDANIEL: No. We were waiting to have those summary judgment motions heard until after the discovery was completed.

THE COURT: You probably waited too long. We are not going to hear these seriatim from each defendant. [p. 58] We'll go on for years and years and years.

MR. GRAHAM: Your Honor, if I could clarify something.

THE COURT: I thought I set a cutoff date for making a motion?

MR. GRAHAM: It was extended by stipulation, Your Honor. The stipulation and order on July 1st is the date of the order, and because of Mr. Seiden's illness, a stipulation was entered into and an order entered that stayed certain of the expert witnesses' depositions and also would allow a second series of summary judgment motions to be brought pursuant to a schedule set forth by the Court. That was the order that was entered.

THE COURT: What do you mean by "to be set forth?"

MR. GRAHAM: To be set by the court.

THE COURT: At what time? At the point after the completion of the discovery?

MR. GRAHAM: It was not contemplated necessarily that the depositions of the experts would be completed, but that once it got to a position where, in essence, the parties realized that they could go forward with their motion for summary judgment, that the motions could be

filed, then pursued to an organized briefing schedule as set by the Court.

[p. 59] MR. SAMET: I would agree with what Mr. Graham said with one modification. I think it was contemplated that the expert discovery would be completed.

In other words, making the motions that we can make now which are unrelated to the expert testimony and that's what we just did now. There remains expert testimony to be completed.

When that is completed, we understood the court would then set another briefing schedule; one schedule, one time for everyone to make the motions if any they want based on the completion of expert discovery.

THE COURT: All right. Go ahead.

MS. McDANIEL: So in summary, Your Honor, to go on and hold the pretrial conference and the meeting of counsel pursuant to local rule 9.4 prior to the hearing of those motions for summary judgment, which may well be dispositive, it seems to be a needless waste of time and expense on all of our behalf.

But beyond that, Your Honor, I would suggest and I think that both Mr. Taylor and Mr. Graham would agree with me that the meeting that they called for this Wednesday is in all respects a preliminary meeting and is not going to be the final and substantive 9.4 meeting that is contemplated by the rules.

In light of that, I would suggest that this [p. 60] meeting which is scheduled for this Wednesday to perhaps be and organizational meeting. I think we are going to need a lot of organization. I think we may well need a

briefing schedule in order to have different sets of defendants exchange preliminarily their statements of fact and contentions of law so that when we are finally able to meet, those meetings can be conducted in a meaningful manner and I would request that for this preliminary meeting that since we have substantial amount of trial counsel on the East Coast that those nonlocal counsel be allowed to participate in this meeting via telephone.

THE COURT: All right.

Mr. Taylor.

MR. TAYLOR: Your Honor, I'd like to keep the scheduling if we could. I agree with the young lady's assessment of the meeting on Wednesday. I don't think it's going to be a traditional 9.4 meeting. I have discussed that with Ms. Hargis and we are going to do what we can.

Because of the number of counsel and because of the number of Your Honor's issues, I would like to be a little more flexible than the rules would ordinarily allow but I would like to get on with the matter and try to hold to the schedule the best we can.

Wednesday, I would like to try to exchange witnesses, at least who we believe we are going to call. I [p. 61] have got a list of exhibits. I hope others do, too.

We can discuss who will be here for trial, what depositions we need to use, how we are going to mark the depositions, what colors we are going to use, various parties are going to use.

There is about 10; so we'll have to select a number of colors to mark the transcripts and how we are going to transmit the transcript, what transcript we are going to

use as a master. There are a number of things we can get accomplished and I'd like to keep it on schedule as much as possible.

That's my position on that issue.

THE COURT: All right. Anybody else want to be heard.

MR. GELFAND: Marty Gelfand appearing for Seymour and Marty Vigman.

I'd like the Court to consider the financial disparity nature of some of the defendants vis-a-vis SIPC and the funding they have. It's going to take some of the defendants a long, long time to review documents and depositions because as of this point, only one of the defendants has copies of everything.

The briefing is something I'd like some additional time so that after we see the documents and read the depositions, we could file meaningful documents with [p. 62] the Court, but the financial problems that many of the defendants have has certainly inhibited us in our preparation and we do need some additional time.

THE COURT: Anybody else? What's the – I am trying to find that motion. What's the date now for the pretrial conference?

MR. TAYLOR: December 5, Your Honor.

THE COURT: December 5.

MS. HARGIS: Yes, sir.

THE COURT: All right.

Mr. Marcus, how much time do you want?

MR. MARCUS: We have requested a continuance, I believe, at least 70 days from the completion of the scheduled depositions, which is sometime in mid November. I would request a continuance of about 60 days or 60 to 90 day range depending on the court's calendar for the pretrial conference, which would push it to sometime around February of 1989.

THE COURT: All right. Anybody else want to be heard?

MR. GRAHAM: One point. There has been a lot of problems as far as the scheduling of expert witness depositions and I'd like the Court to order that as to the remaining expert witness depositions both the plaintiffs and the defendants that the parties enter into a [p. 63] stipulation that become an order as to when those dates – when those depositions would take place and where. I think it might be helpful for everybody.

MR. MARCUS: I am sure that from our point, we'll try to cooperate as much as possible and I believe agreements have been reached in terms of the timing and place of expert depositions.

I don't anticipate that being a problem.

MR. GRAHAM: I'd just like to see that converted to an order so that we have a little more formality as to when these take place because it's too informal as to when they have been scheduled and taken off calendar to accomodate [sic] particular schedules and its been a nightmare for me in keeping track of all the plaintiffs'

experts, as well as we haven't gotten down to the defendants' experts yet.

MR. MARCUS: I am not sure whether Mr. Graham is asking for a specific stipulation of dates and places now or just directed that the parties cooperate and I would have no objection.

MR. GRAHAM: I was asking that the parties cooperate.

MR. MARCUS: I have no objection to that being embodied and I think it's inherent under the responsibility of counsel, under the Court rules and the Rules of Federal [p. 64] Procedure.

THE COURT: You speak about wasted time. It seems to me, you know, it's almost certain to be a waste of time to predicate a summary judgment motion on an expert witness's testimony. I just can't conceive how that couldn't be controverted. So I don't know.

People are planning to make – it sounds like they are – summary judgment motions predicted on expert testimony. I think you are –

MR. MARCUS: I think we are waiting to see what the plaintiffs' expert have to say before we draft the motion, not their own expert's testimony, but the opposing expert testimony that they were trying to get before they drafted their motions.

THE COURT: If expert testimony on either side is going to be relevant to the determination of the summary judgment motion, I just don't see how – I won't even talk about being hopeful about winning the motion or even

spending the time even making the motion. I don't know how it's going to change.

In other words, I can't see how, and I have no idea what they are, but how summary judgment motions that haven't been made yet are going to affect the course of this case.

MR. MARCUS: Your Honor, I believe it's the [p. 65] intent of the parties that all of the summary judgment motions, whether dependent on expert testimony or not, would be made after the completion of the expert testimony.

That was contemplated in the original briefing schedule and everything was delayed because of Mr. Seiden's illness. And the contemplation of the parties as indicated by the stipulation of July 1st stipulation and order was that the parties had the option of moving that back, both the deposition schedule and the scheduling to file the motion for summary judgment, and it was contemplated that once the depositions were completed, the court would establish a briefing and hearing schedule for the summary judgment motions.

I don't think it was contemplated by at least my clients, that there would be – that they would file a summary judgment now and another one later; but, rather, just one motion to be heard all at once. And it was their desire to complete the discovery of the opposition's experts before drafting their motion.

THE COURT: All right. Anybody else want to be heard?

MR. PASH: David Pash. I represent Aerosonic Corporation and Mssr. Frank and Goldman. I'd like to just add my voice in support of the motion to continue the rule 9.4 conference for the reasons indicated; and in addition [p. 66] as far as my client goes, we are still awaiting some supplemental interrogatory responses that go to the issue of what representations are allegedly fraudulent and what acts are in reliance of those representations.

Now I know we are going to get those shortly; in fact, I believe this week; but the fact remains that they are still outstanding and we still have to see what they show before we can determine what issues are going to be outstanding as to our clients and what kind of documents and exhibits are going to be relevant for our purposes.

Once again, it is just one more factor weighing in favor of some continuance in this 70 to 90 day range of the rule 9.4 conference. It's not just the expert testimony in our case. It's the other evidence as well.

MS. McDANIEL: Your Honor, if I might add one point: In defendant Blumenthal's case as well as in Mr. Pash's clients case, it's also a fact that now that this expert discovery is being conducted, suddenly new factual issues are coming to light.

It's not a matter of the defendant's – pardon me – the plaintiff's expert opinion so much as suddenly the facts upon which those opinions are based are suddenly bringing new facts to light and as we raised in our joinder papers, where defendant Blumenthal is concerned, we suddenly learned of new documents which purportedly contain [p. 67] misrepresentations which were never

identified by the plaintiffs before in spite their arguments in opposition to this motion.

I have to say those arguments are somewhat disingenuous because the previous discovery that they referred to just referred to generically to types of documents without referring specifically to documents that they claim misrepresentations were made; and then in the latter discovery responses, they purported to exhaustively identify those documents in which they claim misrepresentations were made and now we have learned through Seiden's deposition that there are more than the 44 documents they specifically identified in those earlier interrogatory responses that they are now belatedly claiming contain misrepresentations; so it's not a matter that we are waiting for expert opinions, but that there may well be other traps for the unweary in those depositions.

Thank you, Your Honor.

MR. TAYLOR: Your Honor, if I may, those are public documents, 10-Ks and 10-Qs and other documents that contained misleading statements. We certainly don't want these parties to claim prejudice because of some alleged failure to release documents at an expert's deposition.

We certainly would work with them to cure any so-called claimed prejudice even though they knew that we [p. 68] were claiming 10-Ks and 10-Qs had generically had contained false statements.

For that reason, and for the reasons I said before, Your Honor, we are happy to work with the defendants to

accommodate their schedules and their problems. There are a lot of us.

So it works two ways, but I'd really like to try to keep the schedule we have; but if we can't do it, we can't do it; but I'd like to get done what we can; and it seems to me if we hold the present schedule and look toward the pretrial conference perhaps as more of a senior status conference with a draft perhaps of a pretrial order, if we haven't been able to reach one, we can do that; but at least try to have a schedule that holds ourselves basically to the fire so we can get things done. These things tend to lead out and lead out and lead out.

THE COURT: All right.

Here's the ruling: I am going to grant the motion to this extent, and I made a note and then I lost it.

I am going to grant. I am going to continue the pretrial conference from December 5 to January 10. I will make it January 17. The reason I make it January 17 is because – excuse me. January 16. Monday, January 16, 3:00 P.M.; and the current date of December 5 has been [p. 69] converted to a status conference because I expect by that time, if they are not already filed – the clerk tells me that's a holiday, January 16.

MR. MARCUS: Martin Luther King's birthday, Your Honor.

THE COURT: I am doing this without a calendar of our 1989. Then I am going to push it back to January 10 at 3:00 P.M. Excuse me. January 9, 3:00 P.M. January 9 at 3:00 P.M. That's a Monday afternoon. Let's see.

We'll make December 5 a status conference and by that time, one, discovery should have been over for several weeks, completed, I would think. I would think they would be completed –

MR. GRAHAM: Your Honor –

THE COURT: – by mid November.

MR. GRAHAM: No. Let me explain the problem. The problem is that in scheduling the depositions of Mr. Seiden and Mr. Torkleson for Mr. Samet, because of his schedule, we have had to carry those into January and, in fact, they don't commence until early January 23rd; so it would be actually three consecutive weeks in January where there would be depositions of the expert witnesses concluding about the second week of February.

However, as I see the local rules, that there would not be an effect under the rules of carrying [p. 70] discovery of the expert witnesses beyond the date of the pretrial conference. So I just want the Court to understand what our schedule is.

THE COURT: Let me ask this question: How much of the pending discovery do you expect to be completed – maybe I should address the defendants – by, say, the end of November?

MR. MARCUS: If I can read Jeffrey Tew's declarations that we expect to complete the depositions of Messrs Foley and Hammershaw sometime in mid November.

There is the issue of reopening discovery. I heard what Mr. Taylor said and he tends to generalize: If the defendants breathe, it's a massive fraud; but the fact is

that under rule nineof [sic] Federal Rules of Civil Procedure, when a defendant is accused of fraud, they are entitled to specificity. This is the statement. Here is where it's made. This is the person who made it and this is the person that he made to it and not just a generic: Well, he made such and such false statements in such and such documents.

The fact is that in interrogatories, we asked them to specify the documents and in response to an interrogatory they supposedly specified the documents and now we discover when their expert takes the stand that there are more documents.

[p. 71] THE COURT: I don't want you to tell me your troubles. I just want to know – remember my question?

MR. MARCUS: The point is that there may be a motion to reopen discovery based on all of these new documents that all of a sudden platinfiss [sic] are now relaying [sic] on which they didn't disclose in prior discovery; so until that motion –

THE COURT: Reopen discovery generally?

MR. MARCUS: As to specific issues raised by that. Other than that, the Dash defendants would be able to complete their expert deposition testimony, I believe, by mid November based on the declaration of Jeffery Tew. I can't speak for the other defendants.

THE COURT: Mr. Samet.

MR. SAMET: I believe discovery, with respect to the Holmes' aspects of the case, probably won't be completed until February or March. The schedule that Mr. Graham

mentioned is, as he indicated; and then following that, they are entitled to depose certain of our expert; so I think discovery would be completed in March, but I would have no objection to the pretrial conference being completed before then because I agree with Your Honor. I don't think much significant summary judgment material would be coming out of that.

THE COURT: What does that mean?

[p. 72] Does that mean that you would be ready to or not – you already made your motion. The other defendants would be ready to brief their motions before the end of discovery? Summary judgment motions, I mean?

In other words, you think you can make your summary judgment motion, say, by sometime in December, if you intend to make them. I am not encouraging it.

MR. MARCUS: We so intend to make it. We do want to complete discovery of the plaintiff's experts before drafting the motions.

We don't think it's necessary for the plaintiffs to finish deposing our experts before we make the motions and I don't know what their scheduling is in that regard.

I assume that Mr. Graham is working that out with Mr. Dubin and I really don't know when they plan on taking the depositions of our experts except that it's after we complete the deposition of their experts.

MR. BONNER: We only have one.

MR. MARCUS: That's true.

THE COURT: Well, I think the only thing I can do at this time is: I am not going to make this open-ended now,

but I am going to abide by that schedule that I mentioned earlier which is to continue the pretrial conference to January 9.

[p. 73] And then we will have a status conference in December to see, you know, whether it makes sense to hold the pretrial conference on that January date, all right, or whether discovery is still going on to such an extent that we ought to continue the pretrial conference further because some people plan on making summary judgment motions which might affect the scope of the issues remaining in the case.

So with that reservation, I am going to grant Mr. Marcus's – it's your motion?

MR. MARCUS: Yes, it was.

THE COURT: Grant the motion of the Dash defendants in part; that is to say, I am going to continue the pretrial conference as I said to January 9 and we'll hold the status conference on December 5.

What time is that December 5?

THE CLERK: 1:30 P.M.

THE COURT: All right.

Anything else?

MR. MARCUS: Should I submit an order, Your Honor?

THE COURT: No.

MS. McDANIEL: Your Honor, with respect to the 9.4 meeting –

THE COURT: Excuse me. The answer is yes.

[p. 74] Yes, the 9.4 meeting?

MS. McDANIEL: – which has been called for this Wednesday, what happens with respect to that and if we continue with that date –

MR. TAYLOR: It's off.

THE COURT: I think 9.4 doesn't say it has to be exactly 40 days before the pretrial conference. You can have it anyway.

MR. MARCUS: Your Honor, if I might make a suggestion: I think Mr. Taylor should start the process. Perhaps we could be scheduling meetings or scheduling dates for exchanges of proposed stipulated facts.

I agree that it shouldn't be necessary for the trial counsel located on the East Coast to have to fly out here Wednesday.

THE COURT: I agree with Mr. Marcus that this case is probably just going to take more than one meeting where the lawyers sit down in somebody's office and they rough out a draft in an hour.

I think you are going to have several meetings and it's not going to hurt getting started on the preliminaries.

MR. TAYLOR: Then we meet on Wednesday.

THE COURT: Since you have a date set, I don't see why you can't start ironing out some of the [p. 75] preliminaries that were mentioned.

MR. MARCUS: I have no problem as long as it's understood that counse [sic] out of town can either be represented by local counsel.

THE COURT: Or be available by phone or participate by conference call. That is perfectly acceptable and I would encourage that. All right.

Anything else?

MR. TAYLOR: Your Honor, I do have one thing more: I'd like to reopen one comment that Mr. Samet made and it does concern me.

THE COURT: Is this on the motion?

MR. TAYLOR: Yes.

THE COURT: All right. Go ahead.

MR. TAYLOR: This involves the National Enterprises that counsel cite in their reply memorandum and I have not had a chance to either argue that case or put a memo in on it and it is not of this circuit but I would like to put in a short brief on that particular case if the Court considers it's important because it does not apply and it should not apply in this case and I have, Heaven knows, several reasons why it should n't.

THE COURT: No. I don't need another brief but I will bear in mind that your position doesn't apply.

MR. TAYLOR: Yes, but I have a reason for it, [p. 76] too.

THE COURT: I am sure you do.

Thank you very much, counsel.

MR. GRAHAM: Thank you, Your Honor.

MR. TAYLOR: Thank you, Your Honor.

MR. SAMET: Thank you, Your Honor.

(Proceedings adjourned).

* * *

I, XAVIER MIRELES, CSR 5001, do hereby certify that the foregoing transcript is true and correct.

/s/ Xavier Mireles 10/29/88
XAVIER MIRELES, CSR 5001 DATE

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
MARK D. LARSEN
SHEPPARD, MULLIN, RICHTER & HAMPTON
A Partnership Including
Professional Corporations
333 South Hope Street, 48th Floor
Los Angeles, California 90071

Telephone: (213) 620-1780

Attorneys for Plaintiff
SECURITIES INVESTOR PROTECTION
CORPORATION

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al., Plaintiffs, v. SEYMOUR VIGMAN, et al., Defendants.	CASE NO. CV 83-4742-AWT (Tx) (Consolidated Cases)
AND CONSOLIDATED ACTIONS	ORDER FOR ENTRY OF FINAL JUDGMENT (AND STAY OF PROCEEDINGS)

CV 83-5674-AWT

CV 87-1679-AWT

FILED
DEC 22 1988

The Motion by the Securities Investor Protection Corporation for Leave to File an Interlocutory Appeal, or, in

the Alternative, for Entry of Final Judgment under Federal Rule of Civil Procedure 54(b) and for a stay of all proceedings pending appellate review came on regularly for hearing before the Honorable A. Wallace Tashima on December 19, 1988 at 9:30 a.m. After consideration of the papers filed in support of and in opposition to the Motion, and the oral argument of counsel, it is hereby

ORDERED that each of the orders granting summary judgment and the summary judgments in favor of defendant Robert G. Holmes Jr., and against plaintiffs, disposing all claims by plaintiffs against defendant Holmes, hereby is amended pursuant to F. R. Civ.P. 54(b) to include an express determination that there is no good reason for delay and an express direction for the entry of judgment.

FUTHER [sic] ORDERED that all further proceedings in this action and in the actions consolidated herewith are stayed pending appeal (if a timely notice of appeal from this final judgement in favor of defendant Holmes is filed) or until otherwise ordered by the Court, except:

1. Any activity, including motions, stipulations and orders, to negotiate and complete any settlements;
2. Motion for entry of default judgment against defendant Lugo and
3. Any discovery activity (primarily depositions) with the prior approval of the court

for good cause shown for an exception from the stay.

Dated: DEC 22 1988

/s/ AWT
A. Wallace Tashima
United States District Judge

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
MARK D. LARSEN
SHEPPARD, MULLIN, RICHTER & HAMPTON
333 South Hope Street, 48th Floor
Los Angeles, California 90071

Telephone: (213) 620-1780

Attorneys for Plaintiff
SECURITIES INVESTOR PROTECTION CORPORATION

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR PROTECTION CORPORATION, et al.,	)	Case No. CV 83-4742-AWT (Tx) (Consolidated Cases)
Plaintiffs,	)	
v.	)	NOTICE OF APPEAL OF PLAINTIFF SECURITIES INVESTOR PROTECTION CORPORATION
SEYMOUR VIGMAN, et al.,	)	
Defendants.	)	
AND CONSOLIDATED ACTIONS.	)	

NOTICE IS HEREBY GIVEN that Plaintiff Securities Investor Protection Corporation ("SIPC)" hereby appeals to the United States Court of Appeals for the Ninth Circuit from the orders filed October 31, 1988 granting the motions of defendant Robert G. Holmes, Jr. for summary judgment, which orders were made final pursuant to Rule 54(b) of the Federal Rules of Civil Procedure pursuant to the Order for Entry of Final Judgment (and Stay of Proceedings) entered by the United States District Court for the Central District of California on December

22, 1988, a copy of which is attached hereto as Exhibit "A".

DATED: January 6, 1989

Stephen C. Taylor
Joseph F. Coyne, Jr.
Mark D. Larsen
Sheppard, Mullin, Richter
& Hampton

By /s/ Stephen C. Taylor
Stephen C. Taylor

Attorneys for Plaintiff
Securities Investor
Protection Corporation

EXHIBIT "A"

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
MARK D. LARSEN
SHEPPARD, MULLIN, RICHTER & HAMPTON
A Partnership Including
Professional Corporations
333 South Hope Street, 48th Floor
Los Angeles, California 90071

Telephone: (213) 620-1780

Attorneys for Plaintiff
SECURITIES INVESTOR PROTECTION
CORPORATION

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

SECURITIES INVESTOR, PROTECTION CORPORATION, et al., Plaintiffs, v. SEYMOUR VIGMAN, et al., Defendants. AND CONSOLIDATED ACTIONS	CASE NO. CV 83-4742-AWT (Tx) (Consolidated Cases) ORDER FOR ENTRY OF FINAL JUDGMENT (AND STAY OF PROCEEDINGS) CV 83-5674-AWT CV 87-1679-AWT FILED DEC 22 1988

The Motion by the Securities Investor Protection Corporation for Leave to File an Interlocutory Appeal, or, in the Alternative, for Entry of Final Judgment under Federal Rule of Civil Procedure 54(b) and for a stay of all proceedings pending appellate review came on regularly for hearing before the Honorable A. Walla-e Tashima on December 19, 1988 at 9:30 a.m. After consideration of the papers filed in support of and in opposition to the Motion, and the oral argument of counsel, it is hereby

ORDERED that each of the orders granting summary judgment and the summary judgments in favor of defendant Robert G. Holmes Jr., and against plaintiffs, disposing all claims by plaintiffs against defendant Holmes, hereby is amended pursuant to F. R. Civ.P. 54(b) to

include an express determination that there is no good reason for delay and an express direction for the entry of judgment.

FUTHER [sic] ORDERED that all further proceedings in this action and in the actions consolidated herewith are stayed pending appeal (if a timely notice of appeal from this final judgment in favor of defendant Holmes is filed) or until otherwise ordered by the Court, except:

1. Any activity, including motions, stipulations and orders, to negotiate and complete any settlements;

2. Motion for entry of default judgment against defendant Lugo and

3. Any discovery activity (primarily depositions) with the prior approval of the court for good cause shown for an exception from the stay.

Dated: DEC 22 1988

/s/ AWT
A. Wallace Tashima
United States District Judge

EXHIBIT "A"

Nos. 89-55094 and 89-55128

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

vs.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

On Appeal From The United States District Court For The Central District Of California Honorable A. Wallace Tashima

PLAINTIFFS-APPELLANTS' OPENING BRIEF

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
JOEL E. BONNER
SHEPPARD, MULLIN, RICHTER &HAMPTON
333 South Hope Street, 48th Floor
Los Angeles, California 90071
Telephone: (213) 620-1780

C. EDWARD SIMPSON
MICHAEL J. ABBOTT
JONES, BELL, SIMPSON & ABBOTT
800 Wilshire Boulevard, Fifth Floor
Los Angeles, California 90017
(213) 485-1555

G. ROBERT BLAKEY
Notre Dame Law School
Notre Dame, Indiana 46556
Telephone: (219) 239-5717
CORNWELL & BLAKEY
1225 Seventeenth Street
Suite 2650
Denver, Colorado 80202
Telephone: (303) 295-2500
Attorneys for Plaintiff-Appellant Securities Investor Protection Corporation

Attorneys for Plaintiffs-Appellants Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated, and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation

CERTIFICATION REQUIRED BY CIRCUIT RULE 28-2.1

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

vs.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

The undersigned counsel of record certify that they are unaware of any parties having an interest in the outcome of this case, apart from the parties herein and the defendants below:

Seymour Vigman
Aero Systems, Inc.
Aerosonics Corporation
Creditbank, Inc.
Dash Industries, Inc.
Haberico, Inc.
Jay Dash
Phillip Dash
Isadore Diamond
Elliot I. Eiseman
Herbert J. Frank
Frankie Mae Garrity

Habers, Inc.
Habers, Inc. Defined Benefit Pension Trust
Ibebafin S.A.
Keops S.A.
Magnetic Technologies Corporation
Talingo Corporation
Tula Corporation
Martin Blumenthal
Jose Luis Calogne, aka Jose Luis Calonge Rivas
Dolores Owens Cipparone, aka Dee Cipparone
David S. Goldman
Jack A. Haber
Robert G. Holmes, Jr.
Joseph A. Lugo, Jr.
Robert J. Mansell
Gordon H. McNeil
Edward P. Prescott
Jose Camprubi Sala
Velma Shaw, aka Velma Shaw Meyers
Nettie Vigman
Lawrence West, aka Larry West

This representation is made to enable the judges of this Court to evaluate possible recusal.

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
JOEL E. BONNER
SHEPPARD, MULLIN, RICHTER & HAMPTON

G. ROBERT BLAKEY
CORNWELL & BLAKEY
Attorneys for Plaintiff-Appellant Securities Investor Protection Corporation

C. EDWARD SIMPSON
MICHAEL J. ABBOTT
JONES, BELL, SIMPSON & ABBOTT
Attorneys for Plaintiffs-Appellants Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated, and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation

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Case Nos. 89-55094 and 89-55128.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

vs.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

On Appeal From The United States District Court For The Central District Of California Honorable A. Wallace Tashima

PLAINTIFFS-APPELLANTS' OPENING BRIEF

I

PRELIMINARY STATEMENT

This appeal arises from a summary judgment for defendant Robert G. Holmes, Jr. ("Holmes") on claims for violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO") (18 U.S.C. § 1961 *et seq.*) (1982),

the Securities Exchange Act of 1934 (15 U.S.C. § 78a *et seq.*) (1970), common law breaches of fiduciary duty, and fraud.

Holmes independently, and with others, orchestrated and participated in a complex scheme to manipulate unlawfully six over-the-counter securities that caused the failures of two securities brokerage firms, First State Securities Corporation ("FSSC") and Joseph Sebag Incorporated ("Sebag") and the loss of brokerage customers' securities and cash.[1] As a result of these failures, the appropriate district courts, under the Securities Investor Protection Act of 1970, as amended,[2] ("SIPA") appointed Laurence A. Schroeder (as Successor to John L. Britton) and Eugene W. Bell as trustees to liquidate FSSC and Sebag (the "Trustees").

As a direct result of the acts of Holmes,[3] alone and in concert with his long-time confederates, the plaintiff

[1] Holmes and his co-defendants manipulated the six securities issued by Aero Systems, Inc., Aerosonics Corporation, Bunnington Corporation, Creditbank, Inc., Dash Industries, Inc., and Osrow Products Corporation (hereinafter the "Target Securities").

[2] 15 U.S.C. § 78aaa *et seq.*

[3] Holmes is the founder, President, Chief Executive Officer, Director and major shareholder of Aero Systems, Inc. ("Aero Systems"), an airplane used parts dealer in Miami, Florida. Clerk's Record ("C.R.") 1317, pp. 4-5. Aero Systems stock was manipulated by Holmes, (C.R. 1310, pp. 13-15) as was the stock of Bunnington Corporation ("Bunnington"). C.R. 1310, pp. 37-43. Bunnington's major shareholders were co-conspirator Vigman and Vigman's co-conspirator brother-in-law, Isadore Diamond. C.R. 1317, pp. 31 & 37.

Trustees and plaintiff Securities Investor Protection Corporation ("SIPC") have sustained damages of approximately $12.5 million.[4]

Holmes moved for summary judgment asserting a lack of causation between Holmes' conduct and injuries to SIPC and the Trustees. He also contended that SIPC lacked standing to assert claims under RICO because SIPC is not a "purchaser or seller" of securities. By its rulings entered October 31, 1988, the District Court granted Holmes' motions for summary judgment on these bases from which this appeal is taken.[5]

[4] The Appeals before this Court have been consolidated, resulting in this joint brief filed pursuant to Ninth Circuit Rule 28.4. In addition, and with leave of this Court, the Trustees present a supplemental brief.

[5] C.R. 1344, p. 2; C.R. 1343, p. 3. In addition to the causation and RICO orders, the Court entered a third order on October 26, 1988 that SIPC "lacks standing" to assert claims against Holmes under Section 10(b) and Rule 10b-5. Order of Partial Summary Judgment, C.R. 1341, p. 2. The Court's basis for summary judgment on such grounds, in light of the law of the case found in *SIPC v. Vigman*, 803 F.2d 1513 (9th Cir. 1986), is found in the Court's handwritten modification of Holmes' conclusions of law which states: "6. There is no evidence (SIPC having the burden under *Celotex*) that any pledge of fully-paid-for customer stock was 'unauthorized.' " C.R. 1340, p. 6.

Plaintiffs disagree with the Court's conclusion. SIPC's evidence of unauthorized pledges of securities by FSSC presented a triable issue of material fact. The Court misapplied the applicable burden of proof to SIPC's evidence. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 25[illegible] (1986); *United Steel Workers of America v. Phelps Dodge Corp.*, 865 F.2d 1539, 1542 (9th Cir.

(Continued on following page)

With respect to the RICO claims, the District Court modified Holmes' proposed findings to find expressly that there *was a genuine dispute regarding material facts* with respect to *all* of the substantive RICO issues including, *inter alia*:

> (1) Whether or not Holmes invested income in an enterprise;
>
> (2) Whether or not Holmes acquired an interest in an enterprise;
>
> (3) Whether or not Holmes conducted the affairs of an enterprise through a pattern of racketeering activity;
>
> (4) Whether or not the predicate acts alleged constitute fraud in the sale of securities, mail fraud or wire fraud; and
>
> (5) Whether or not two predicate acts occurred within ten years of each other and constitute a "pattern".[6]

(Continued from previous page)

1989). The only evidence presented to the Court on the issue of unauthorized pledges, and the only rational inferences to be drawn therefrom, reveal that FSSC improperly pledged a large volume of customer paid securities without authorization in order to receive instant loan funds from Stock Clearing Corporation of Philadelphia. C.R. 1293, pp. 4-6. As a consequence, the Court erred in granting Holmes summary judgment based on a perceived lack of evidence of unauthorized pledges of securities.

By its ruling in 1986, this Court severely limited the securities laws as they could be used by SIPC. SIPC's ability to use RICO to remedy massive fraudulent securities manipulations as occurred here must not be so limited.

[6] C.R. 1343, pp. 2-3, ¶¶ 2-4, 6 and 7.

Significantly, by the same findings, the Court found that:

> (1) There *is* a genuine issue of material fact that "Holmes conspired to violate RICO Sections 1962(a), 1962(b), or 1962(c),"[7] and:
>
> (2) There *is* a genuine issue of material fact whether or not the predicate acts caused "the injuries" of SIPC and/or the Trustees.[8]

The District Court unequivocally recognized, then, that plaintiffs presented substantial material evidence that Holmes violated *all* substantive sections of RICO, and that the violations, in fact, caused plaintiffs' damage. Yet, the Court inexplicably held in the same findings, that:

> (1) "The grant of summary judgment on 'causation' applies also to the RICO claims."[9] and;

---

[7] *Id.* ¶ 5.

[8] *Id.* ¶ 8.

[9] The Court's reference to the granting of Holmes' motion regarding a lack of causation is to the Statement of Uncontroverted Facts and Conclusions of Law regarding causation and provides, in pertinent part, as follows:

> "The proximate cause requirement under RICO (citation) is, in substance, no different than the "loss causation" requirement under the securities laws, when the predicate acts on which the RICO violation is based is securities fraud. *E.g., Sperber v. Boesky*, 849 F.2d 60 (2d Cir. 1988)."

C.R. 1342, p. 10, ¶ 23.

> (2) "SIPC does not meet the 'purchaser-seller' requirements for standing to assert RICO claims . . . predicated on violations of Section 10(b) and Rule 10b-5 of the 1934 Securities Exchange Act."[10]

The Court erred, then, when it granted summary judgment for a lack of causation because it specifically found that, as far as the RICO claims are concerned, *a triable issue of fact as to causation was presented*. Such a finding by the Court was proper in the first instance as the facts before it overwhelmingly supported the finding, as will be shown below. The Court erred by wrongfully implying the Section 10(b) and Rule 10b-5 "purchaser-seller" requirement (also part of the implied claim for relief in those statutes) into the broad, express "any offense . . . involving fraud in the sale of securities" language of RICO.[11] Further, no acceptable jurisdiction was offered for the similar implication of such limitations into the claims for relief based on mail and wire fraud under RICO.

On December 22, 1988, the District Court entered its order directing that final judgment be granted as to Holmes under Rule 54(b) of the Federal Rules of Civil Procedure. On January 6 and January 20, 1989, SIPC and the Trustees respectively timely filed their Notices of Appeal. The appeals were consolidated.

---

[10] Order Granting Summary Judgment (RICO claims), C.R. 1343, p. 3.

[11] 18 U.S.C. § 1961, *et seq*.

Plaintiffs respectfully urge this Court to reverse the District Court's summary judgment and allow plaintiffs to try their case against Holmes.[12]

II

STATEMENT OF ISSUES

(1) Did the District Court err in granting summary judgment to Holmes, when it held that plaintiffs did not present a triable issue of material fact that the unlawful conduct of Holmes alone and/or Holmes' conduct in league with his co-conspirators was the proximate cause of damage to the Trustees or SIPC under 18 U.S.C. Section 1964(c)? (Yes)

(2) Did the District Court err in granting summary judgment to Holmes, when it held that SIPC must be a "purchaser or seller" of securities to maintain an action under 18 U.S.C. Section 1964(c) for conduct consisting of (a) "any offense . . . involving fraud in the sale of securities . . . punishable under any law of the United States," (b) wire fraud or (c) mail fraud in violation of 18 U.S.C. Section 1962? (Yes)

---

[12] Plaintiffs' evidence presented in opposition to Holmes' Motions of Summary Judgment is contained in the Statement of Background and Facts. C.R. 1317. The Statement of Background and Facts is too lengthy to be recited here. Plaintiffs urge the Court to review it beyond its citation in this brief to appreciate more fully Holmes' role in the fraudulent scheme and conspiracy at issue.

III

JURISDICTION AND STANDARD OF REVIEW

A. Jurisdiction.

Jurisdiction in the District Court was based upon federal questions arising under RICO, 18 U.S.C. Section 1961 through Section 1968, the Securities Exchange Act of 1934, 15 U.S.C. Section 78a through Section 78hh-1, and 28 U.S.C. Section 1331. The District Court also exercised jurisdiction over the state and common law claims alleged in the First Amended Complaint by virtue of its pendent jurisdiction. The bases for jurisdiction over SIPC's and the Trustees' appeals from the grant of summary judgments in favor of Holmes are 28 U.S.C. Section 1291 and Federal Rule of Civil Procedure 54(b), and the appeals were consolidated.

B. Standard Of Review

As recognized by the Supreme Court in *Anderson v. Liberty Lobby, Inc.*,[13] plaintiffs' burden in resisting Holmes' motions was only to present that quantum of evidence which, taken together with all favorable inferences, would be sufficient for a jury to return a verdict in plaintiffs' favor. Review of the granting of such a motion is *de novo*, and all inferences must be drawn in favor of the non-moving party.[14]

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[13] 477 U.S. 242 (1986).

[14] *Wood v. Ostrander*, 851 F.2d 1212, 1213 (9th Cir., 1988); *Leer v. Murphy*, 844 F.2d 628, 631 (9th Cir. 1988); *Medallion*

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The Supreme Court in *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, stated that the non-moving party "must do more than show that there is some metaphysical doubt as to the material facts."[15] Once the non-moving party presents evidence that is plausible and beyond "some metaphysical doubt," the District Court must consider all "justifiable" and "legitimate" inferences in favor of the non-moving party.[16] The District Court must also keep in mind that "[c]redibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from facts are jury functions, not those of a judge. . . . The evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in his favor."[17]

This Court holds that "a justifiable inference" is not "the most likely inference or the most persuasive inference."[18] Indeed, a justifiable inference is any inference that is "rational" or "reasonable."[19]

In this case, the evidence that Holmes was a principal, co-conspirator and aider and abettor in the manipulation of the prices of Bunnington and Aero Systems

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Television Enters., Inc. v. SelecTV of California, Inc., 833 F.2d 1360, 1362 (9th Cir. 1987), *cert. denied*, 109 S. Ct. 3241 (1989).

[15] 475 U.S. 574, 586 (1986).

[16] *Id.* at 587-8.

[17] *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986).

[18] *United Steel Workers*, 865 F.2d at 1542.

[19] *Id.*; *See also T.W. Elec. Serv. v. Pacific Elec. Contractors*, 809 F.2d 626 (9th Cir. 1987).

stocks, and in the scheme to manipulate them, not only presents jury questions, but is overwhelming.

IV

STATEMENT OF THE CASE

A. SIPC And Its Trustees Serve Important Public Interests And Must Be Allowed To Use RICO To Assist In The Regulation Of The Securities Market.

In 1970, the same Congress that enacted RICO created SIPC as a nonprofit membership corporation established under SIPA in response to the collapse of numerous brokerage houses in order to provide greater protection for customers of registered brokers, dealers and members of national securities exchanges.[20] To bolster public investor confidence, Congress broadly analogized to the federal corporations that ensure savings and demand deposits[21] and enacted the new program, which was jointly sponsored by the securities industry and the Securities and Exchange Commission ("Commission").[22] The several purposes of that program, were:

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[20] 15 U.S.C. § 78ccc; S. Rep. No. 1218, 91st Cong., 2d Sess. 3 (1970) ("Senate Report"); H.R. Rep. No. 1613, 91st Cong. 2nd Sess. ("House Report"), reprinted in 1970 U.S. Code Cong. & Admin. News, 5254, 5254-55. Membership in SIPC is automatic upon registration as a broker or dealer with the Securities and Exchange Commission under Section 15(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78ccc(a).

[21] Senate Report at 4.

[22] House Report at 28; Hearings on S. 2348, S. 3988, S. 3989 Before the Subcomm. on Securities of the Senate Comm. on

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> " . . . to protect individual investors from financial hardship; to insulate the economy from the disruption which can follow the failure of major financial institutions; and to achieve a general upgrading of financial responsibility requirements of brokers and dealers to eliminate, to the maximum extent possible, the risks which lead to customer loss."[23]

SIPA accomplished these purposes essentially by two methods. First, it enhanced the Commission's powers to establish financial responsibility rules for brokers and dealers[24] and to impose on the self-regulatory organizations[25] requirements for the financial examination of their members.[26] Second, it established SIPC, which it empowered, among other things, to commence proceedings for the liquidation of its members whose financial condition posed the threat of loss to their customers.

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Banking and Currency, 91st Cong., 2d Sess. 12 (1970). Hearings on H.R. 13308, H.R. 17585, H.R. 18081, H.R. 18109, H.R. 18458 Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce, 91st Cong., 2d Sess. 330 (1970). These hearings will hereinafter be cited as "Senate Hearings" and "House Hearings."

[23] Senate Report at 4; *see also* House Report at 1.

[24] 15 U.S.C. § 78ggg(a).

[25] "Self-regulatory organizations" consist of national securities exchanges and the National Association of Securities Dealers, Inc. ("NASD").

[26] 15 U.S.C. § 78iii(f). Similarly, SIPC is given responsibility to work with the self-regulatory organizations towards the standardization of their examining procedures and the development of procedures for the early detection of approaching financial difficulty of SIPC members. 15 U.S.C. § 78iii(c).

Referring to the several aims of SIPA, the United States Supreme Court has stated: "The Act apportions responsibility for these tasks among the SEC, the securities industry self-regulatory organizations, and SIPC. . . . "[27]

Lower federal courts, too, recognize the important public function served by SIPC and its trustees: "Although not formally part of the federal government, SIPC and its trustees vindicate important public interests."[28]

The District Court's ruling, if allowed to stand, will deprive SIPC of an effective tool to correct abuses in massive fraud cases of this type, in which an ordinary individual private party simply would not have the financial staying power to bring miscreants such as Holmes to account.[29]

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[27] *SIPC v. Barbour*, 421 U.S. 412, 415-16 (1975).

[28] *In re Application of Executive Secs. Corp.*, 702 F.2d 406, 410 (2d. Cir.), *cert. denied*, 464 U.S. 818 (1983).

[29] The District Court's decision also constitutes a potential impediment to the fulfillment of the President's pledge, *infra*, note 30, as both the FSLIC and FDIC use RICO in carefully selected bank fraud litigation. *See e.g., FSLIC v. Shearson-American Express, Inc.*, 658 F. Supp. 1331 (D.P.R. 1987); *FDIC v. Hardin*, 608 F. Supp. 348 (E.D. Tenn. 1985). *See generally Combating Fraud, Abuse and Misconduct in the National's Financial Institutions: Current Federal Efforts are Inadequate*, H.R. Rep. No. 1088, 100th Cong. 2d Sess. 2-13 (1988) (Criminal misconduct by insiders is a major contributing factor in approximately one-third of all commercial bank failures and three-fourths of all thrift failures; loss estimates range from $31 to $80 billion). State insurance commissioners also are using RICO, in carefully selected litigation, to vindicate the interests of those who

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SIPC's role in the securities industry is, moreover, directly paralleled by that of similar agencies facing the white-collar-crime crisis threatening to engulf the banking and thrift industry,[30] the insurance industry[31] and the

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have been defrauded. *See e.g., Schacht v. Brown*, 711 F.2d 1343, 1356-58 (7th Cir.), *cert. denied*, 464 U.S. 1002 (1983). The District Court's judgment, too, could undermine those public-purpose projects.

[30] The President, for example, told the Nation on February 6, 1989 that "unconscionable risk-taking, fraud and outright criminality . . . [were] factors" that led to the crisis in the savings and loan industry. *New York Times*, Feb. 7, 1989, at 31, col. 1. He promised "every effort to recover assets diverted from these institutions and to place behind bars those who had caused losses through criminal behavior." *Id. Office of Comptroller of the Currency, Bank Failure: An Evaluation of the Factors Contributing to the Failure of National Banks* (1988) (insider abuse significant factor in 35% of the bank failures); *New York Times*, March 11, 1989, at 17, col. 1 (FSLIC fund liabilities exceed assets by $56 billion, four times the total of a year ago). *See generally* Note, *Insider Abuse and Criminal Misconduct in Financial Institutions: A Crisis*, 64 Notre Dame L. Rev. 222 (1989).

[31] The insurance industry, another key component of financial markets, is primarily regulated and protected at the state level; it is facing a similar crisis, particularly in the southwest. In 1987, 234 companies were in liquidation, and 74 companies were in reorganization. *Wall Street Journal*, Nov. 8, 1988, at 12, col. 6. State guaranty funds paid out a record $909 million in 1987 – to bail out the failures. *Id.*, Feb. 17, 1989, at 1, col. 6. "Autopsies of several failed insurers across the country have turned up evidence of frauds and inadequate regulations." *Id.*

pension guaranty field.[32] As such, the District Court's narrow reading of RICO threatens more than the rights of victims of crime in the securities industry.

B. Congress Has Legislated SIPC's Role As Protector Of The Investing Public's Interest.

This appeal must be considered in the context of SIPC's functions within the securities industry.

Congress recognized the importance of SIPC's function of providing for protection of investors by requiring SIPC to establish a fund through assessments upon its members,[33] and by authorizing SIPC to borrow against

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[32] Equally disturbing, if not more so, are the similar prospects for the Pension Benefit Guaranty Corporation ("PBGC"), which insures 31 million workers and retirees in 10,000 single employee pension funds and 8.2 million workers in 2,300 multi-employer plans. In 1987, $1.6 trillion were held in pension plan assets. Yet 1987 also marked "the largest deficit . . . and the most threatening crisis . . . [in the] 13-year history" of the PBGC. *Pension Benefit Guaranty Corporation, Annual Report to the Congress Fiscal Year 1987* at 3. Here, too, "a national tragedy is in the making." 134 Cong. Rec. H. 1072 (March 22, 1988 daily ed.) (statement of Rep. Conyers). Employment and Retirement and Security Act "alone is not able effectively to protect the plans from fraud and misuse and . . . hard-earned money at substantial risk. *Id. See e.g., Thornton v. Evans*, 692 F.2d 1064, 1065 (7th Cir. 1982) (pension plan fraud) ("Evidence . . . traces a pattern which seems distressingly prevalent today: the savings of working men and women are pilfered, embezzled, parlayed, mismanaged and outright stolen by unscrupulous persons occupying positions of trust and confidence.")

[33] 15 U.S.C. § 78ddd.

the United States Treasury up to $1 billion should the SIPC fund be inadequate.[34]

SIPA contemplates that customers' claims resulting from a failed broker-dealer will be satisfied to the maximum extent possible not from the SIPC fund but from the remaining assets held by the failed broker-dealer constituting a "fund of customer property,"[35] in which all customers share ratably to the exclusion of general creditors.[36] SIPC funds supplement the fund of customer property within the limits and manner provided by SIPA.[37]

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[34] 15 U.S.C. § 78ddd(f)-(h).

[35] 15 U.S.C. § 78lll(4); 15 U.S.C. § 78fff-2(c)(1). Procedurally, a SIPC trustee marshals the assets of the failed broker-dealer and creates a "fund of customer property." The fund consists of cash and securities held by the failed broker-dealer for customers. 15 U.S.C. § 78lll(4). The fund does not include securities registered in the customer's name. 15 U.S.C. § 78lll(3)-(4). Thus, in a SIPA liquidation, a customer has any securities registered in his own name returned to him; a customer's "street-name" securities and cash in the customer's account are thrown into the common "fund of customer property."

[36] 15 U.S.C. § 78fff-2(c)(1). Before SIPA, customers only received their pro rata share of the fund (then called "single and separate fund," now called the "fund of customer property"). As for unpaid balances, customers shared with general creditors in the general estate. *See* 3 *Collier on Bankruptcy* §§ 60.73-60.76 (14th ed. 1977). Because of the usually inadequate fund, customers suffered losses. Congress moved to remedy this by setting up SIPC and its fund to make customers as whole as possible within the limits of SIPA.

[37] SIPC may advance up to $500,000 to each customer for the amount by which such customer's "net equity" exceeds his

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Regardless of the extent of assets of the failed firm, each innocent customer with a valid claim for stock or cash is assured of protection by SIPC within statutory limits.[38] Thus, a significant part of the business of SIPC is

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pro rata share of the fund of customer property, and in no event more than $100,000 for that portion of a claim that is for cash. 15 U.S.C. § 78fff-3(a)(1). "Net equity" is simply the filing date value of securities and cash the failed broker-dealer owes the customer less any amount the customer owes the broker-dealer. 15 U.S.C. § 78lll(11). For example, if the fund of customer property totaled $100,000 and the total value of the net equities of all of the customers was $1 million, the customers would share the $100,000 on a pro rata basis and SIPC would supplement the fund for each customer (over what the customer received from the fund) to the statutory limits.

[38] Customers of the two failed brokerages generally break down into two major groups – those who purchased manipulated Target Securities and those who did not. Their ability to recover losses against manipulators are widely disparate under federal law.

Customers who purchased Target Securities share in the fund of customer property, receive reimbursement from SIPC to the extent that the fund of customer property cannot satisfy the customers' net equity claim, and have an action based on Rule 10b-5 or RICO against the manipulators for the difference in price between the Target Securities as manipulated, and the price of the Target Securities, post collapse, minus what the customer has received from the fund and SIPC. Indeed, a class action consisting only of purchasers and sellers of Target Securities has been certified and in consolidated with this case for purposes of discovery. *Cain v. Vigman, et al.*, Case No. CV 83-5674-AWT (Tx).

Customers who did not purchase the Target Securities also share in the fund of customer property and receive a

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to advance funds as required by federal statute to satisfy within the limit of the law the claims of investors whose broker-dealer was injured by the acts or fraudulent manipulations of others. Once SIPC has advanced monies to satisfy customers' claims, SIPC is subrogated to the claims of such customers, including claims against third parties.[39]

In this case, in July 1981, the net capital of FSSC and Sebag fell below the statutory limits and SIPC, pursuant to its statutory obligations, applied to the Court for the appointment of trustees to liquidate the firms under SIPA.[40]

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reimbursement from SIPC to the extent that their net equity claims are not satisfied by the fund. However, these customers could not pursue a Rule 10b-5 action against the manipulators, because they neither bought nor sold the Target Securities. With SIPC, this class of customers is virtually made whole, and SIPC succeeds to their rights. Nevertheless, under the District Court's decision, an anomaly is produced. This class of customers, whose rights SIPC now asserts, were victimized by conduct that undoubtedly could be made the subject of a federal RICO criminal prosecution, in which they would be the complaining witnesses. But because they are not "purchasers or sellers" of the Target Securities, neither they nor SIPC have a civil claim for relief for their losses under RICO, a result hard to justify under a statute that *expressly* provides for criminal *and* civil sanctions to vindicate its violation.

[39] 15 U.S.C. § 78fff-3(a).

[40] A net capital deficiency is determined in accordance with SEC Rule 15c3-1, 17 C.F.R. 240.15c3-1. Under the Rule, a broker-dealer's liabilities, or "aggregate indebtedness," may not exceed its net capital by more than 1500%. "Net capital" is

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Thereafter, SIPC, as is statutorily required, and as a direct result of the acts of Holmes and his confederates, advanced approximately $12.5 million to the Trustees of Sebag and FSSC to pay proper customer claims, to purchase securities in the open market, to satisfy proper customer claims, and to pay other costs and expenses of liquidation.[41] Further, SIPC is subrogated to the rights of each customer who received benefits by virtue of SIPC's advances.

V

ARGUMENT

A. RICO Provides A Critical Statutory Framework For SIPC To Protect Itself From Massive Stock Manipulations.

1. The Background Of RICO.[42]

The legislative history of RICO demonstrates beyond doubt that "Congress wanted to reach both 'legitimate'

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calculated as net worth less downward provisions for non-liquid assets, missing securities, inventory "haircuts" and other risk associated factors. C.R. 1310, p. 20 ¶ 32 n.7. On July 24, 1981, FSSC had a net capital deficiency of $2,634,976. C.R. 1310, p. 36, ¶ 86. The deficiency was caused in substantial part by the acts of Holmes. C.R. 1310, p. 34, ¶ 80.

[41] C.R. 1317, p. 109.

[42] *See generally* Blakey & Gettings, *Racketeer Influenced and Corrupt Organizations (RICO): Basic Concepts – Criminal and Civil Remedies*, 53 Temp. L. Q. 1009 (1980) (hereinafter "Basic Concepts"); Blakey, *The RICO Civil Fraud Action in Context*, 68 Notre Dame L. Rev. 237 (1982) (hereinafter "Civil Action"); Blakey & Cessar, *Equitable Relief Under Civil RICO*, 62 Notre Dame L. Rev. 526 (1987) (hereinafter "Equitable Relief").

and 'illegitimate' enterprises."[43] "[C]ourts and . . . commentators have persuasively and exhaustively explained why . . . RICO . . . [is not limited to] organized crime . . . ".[44] "The occasion for Congress' action was the perceived need to combat organized crime. But Congress for *cogent* reasons chose to enact a more general statute, one which . . . was *not* limited in application to organized crime."[45]

2. Standards Of Unlawful Conduct Under Civil RICO.

Congress directed that RICO "be liberally construed to effectuate its remedial purposes."[46] The directive is a "mandate."[47] Accordingly, the language of the statute is to be read in the same fashion, whether the suit is criminal or civil.[48]

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[43] *H.J., Inc. v. Northwestern Bell Telephone Co.*, 57 U.S.L.W. 4951, 4956 (June 26, 1989), citing *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 495 (1985) ("not just mobsters").

[44] *Owl Const. Co. v. Ronald Adams Contractor, Inc.*, 727 F.2d 540, 542 (5th Cir.), *cert. denied*, 469 U.S. 831 (1984).

[45] *H.J., Inc.*, 57 U.S.L.W. at 4955 (emphasis added).

[46] 84 Stat. 947 (1970). *Sedima*, 473 U.S. 479 at 498 (1985); *Russello v. United States*, 464 U.S. 16, 27 (1983) ("[T]his is the only substantive federal criminal statute that contains such a directive . . . ").

[47] *Lou v. Belzberg*, 834 F.2d 730, 737 (9th Cir. 1987), *cert. denied*, 108 S. Ct. 1302 (1988) quoting *Sedima*, 473 U.S. at 492, n. 10.

[48] *H.J., Inc.*, 57 U.S.L.W. at 4954-56; *Sedima*, 473 U.S. at 489; *Cf. Northern Securities Co. v. United States*, 193 U.S. 197, 401

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At 18 U.S.C. Section 1962, Congress set forth "standards" of "unlawful" conduct, which are enforced through "criminal" and "civil" sanctions. Section 1963 sets out the criminal remedies, and Section 1964 establishes the civil remedies.[49] Because the civil scope of RICO is broader than its criminal scope, RICO is *not* primarily criminal and punitive, but primarily civil and remedial. As the Supreme Court recently stated: "Congress drafted RICO broadly enough to encompass a wide range of criminal activity, taking many different forms and likely to attract a broad array of perpetrators operating in many different ways."[50] RICO must be "read broadly . . . to effectuate its remedial purpose."[51] The burden of proof of showing a Civil RICO violation is proof by a preponderance of the evidence.[52]

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(1904) (Holmes, J., dissenting) ("The words cannot be read one way in a suit which is to end in fine and imprisonment and another way in one which seeks an injunction.").

[49] *Sedima*, 473 U.S. at 489; *Basic Concepts*, 53 Temp. L.Q. 1009 at 1021 n.71; *Civil Action*, 68 Notre Dame L.Rev. 237 at 243 n.20. *See also* 115 Cong. Rec. 6993 (1969) (statement of Sen. Hruska) ("The criminal provisions are intended primarily as an adjunct to the civil provisions, which I consider as the more important feature of the bill."); 116 Cong. Rec. 602 (1970) (statement of Sen. Hruska) ("The principal value of this legislation may well be found to exist in its civil provisions").

[50] *H.J., Inc.*, 57 U.S.L.W. at 4956.

[51] *Sedima*, 473 U.S. at 497-98; *United States v. Turkette*, 452 U.S. 576, 593 (1981) ("both preventive and remedial").

[52] *United States v. Cappetto*, 502 F.2d 1351, 1357 (7th Cir. 1974), *cert. denied*, 420 U.S. 925 (1975) (government suit); *Wilcox*

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3. Section 1964(c): RICO's Private Enforcement Mechanism.

The enforcement mechanism for private litigants under RICO, 18 U.S.C. Section 1964(c), provides:

> "Any person *injured in his business* or property by reason of a violation of section 1962 . . . may sue therefore in any appropriate United States district court and shall recover threefold the damages he sustains and the costs of the suit, including a reasonable attorney's fee."

18 U.S.C. § 1964(c) (emphasis added).

These provisions of RICO were modeled on, but are not identical to, the antitrust laws.[53] Like the antitrust laws, RICO creates "a private enforcement mechanism that . . . deter[s] violators and provide[s] ample compensation to the victims . . . "[54]

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v. First Interstate Bank of Oregon, 815 F.2d 522, 530-532 (9th Cir. 1987) (private suite); *Sedima*, 473 U.S. at 491 ("[N]o indication that Congress sought to depart from [preponderance]").

[53] S. Rep. No. 617, 91st Cong., 1st Sess. 81 (1967); H.R. Rep. No. 1549, 91st Cong. 2d Sess. 56-60 (1970). A private "treble-damages remedy [is needed] . . . precisely for the purpose of encouraging *private* challenges to antitrust violations." *Reiter v. Sonotone Corp.*, 442 U.S. 330, 344 (1979) (emphasis in original).

[54] *Blue Shield of Virginia v. McCready*, 457 U.S. 465, 472 (1982). RICO and the antitrust statutes are well integrated. "There are three possible kinds of force which a firm can resort to: violence (or threat of it), deception, or market power." C. Kaysen & D. Turner, *Antitrust Policy* 17 (1959). RICO focuses on the first two; antitrust focuses on the on the third. *See Agency Holding Corp. v. Mally-Duff & Associates, Inc.*, 483 U.S. 143, 151

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B. The District Court Erred When It Held That Plaintiffs Did Not Present A Triable Issue Of Material Fact That Holmes And His Co-Conspirators' Conduct Was The Proximate Cause Of Its Damage Under 18 U.S.C. Section 1964(c).

1. The District Court Erred By Applying Section 10(b) "Loss Causation" Principles To Plaintiffs' RICO Claims.

Section 1964(c) provides for recovery for injury to property or business "by reason of" a violation of Section 1962. " '[B]y reason of' . . . simply imposes a proximate cause requirement on plaintiffs."[55] In *Haroco*, the Seventh Circuit held:

> "The criminal conduct in violation of section 1962 must . . . have injured the plaintiff's business or property. . . . This causation requirement might not be subtle, elegant or imaginative, but . . . it is based on a straightforward reading of the statute as Congress intended it to be read."[56]

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(1987) ("private attorneys general [for] a serious national problem for which public prosecutorial resources are deemed inadequate"); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 241, *reh'g denied*, 483 U.S. 1056 (1987) ("vigorous incentives for plaintiffs to pursue RICO claims"); *Sedima*, 473 U.S. at 493 ("[p]rivate attorney . . . provision . . . designed to fill prosecutive gaps"). *See generally* Note, *Treble Damages Under RICO*, 61 Notre Dame L. Rev. 526, 533-534 (1986) ("a powerful mechanism in the effort to vindicate the interests of those victimized by crime").

[55] *Haroco, Inc. v. Am. Nat'l Bank and Trust Co.*, 747 F.2d 384, 398 (7th Cir. 1984), *aff'd*, 473 U.S. 606 (1985).

[56] *Haroco* at 398.

As such, a plaintiff, to recover under RICO, need only prove:

> (1) a violation of section 1962 . . . , and
>
> (2) an injury . . . resulting from some or all of the activity comprising the violation(s).[57]

The "by reason of" language appears in several similar federal statutes.[58] In *Mead v. Retail Clerks Int'l Ass'n Local No. 830*,[59] this Court considered Section 303 of the Labor Management Relations Act of 1947, 61 Stat. 158, which is especially relevant since it, too, was "drawn directly from the treble damage provision of the Clayton Act . . . ," and the Court found that the statute, like RICO, "was enacted as an alternative to" using the antitrust laws directly.[60]

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[57] *Marshall & Ilsley Trust Co. v. Pate*, 819 F.2d 806, 809 (7th Cir. 1987). Congress modeled Section 1964(c) on the antitrust acts. *Sedima*, 473 U.S. at 486-487. However, it did not want RICO unduly circumscribed by special antitrust proximate cause limitations. *Id.* at 498-499 ("previous proposal . . . [came] to grief . . . precisely because it could create inappropriate . . . obstacles in the way of . . . a private litigant . . . on questions such as 'standing to sue' and 'proximate cause.' ") (quoting ABA Comments at 115 Cong. Rec. 6995 (1969)); *Lou v. Belzberg*, 834 F.2d at 737 ("not . . . intended to incorporate all of the baggage")).

[58] *See e.g.*, 12 U.S.C. § 1975; 15 U.S.C. § 72; 19 U.S.C. § 1671d(b)(1); 22 U.S.C. § 2399(b)(a); 29 U.S.C. § 186; 31 U.S.C. § 3729; 41 U.S.C. § 119; 46 U.S.C. § 1227.

[59] 523 F.2d 1371 (9th Cir. 1975).

[60] *Id.* at 1376.

In *Mead*, this Court held that "the 'by reason of' language is read as incorporating common law principles of causation."[61] This Court further held that injury occurs 'by reason of' particular unlawful conduct if such conduct 'materially contributed' to the injury . . . or was a 'substantial factor' in bringing it about *'notwithstanding other factors contributed also. . . . '* "[62]

In contrast, causation principles under Rule 10b-5 are judicially restricted because of the "in connection with" requirement, the absence of an express private right of action under Section 10(b),[63] and the efforts of courts to prevent sellers of securities from acting as insurers of every downturn in the price of a buyer's stock.[64]

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[61] *Id.*

[62] *Mead*, 523 F.2d at 1376 (emphasis added). " 'Proximate cause' . . . is merely the limitation which the courts have placed upon the actor's responsibility for the consequences of the actor's conduct." W. Prosser & R. Keeton, *The Law of Torts* § 41 (5th ed. 1984). Under the "substantial factor" test, proximate cause is usually an issue for the jury, "unless the issue is so clear that reasonable persons could not differ." *Id.* That a defendant's conduct can be the legal or proximate cause of harm to a plaintiff if such conduct is a "substantial factor" in causing the harm is supported by the Restatement (Second) of Torts, Section 431. *See also In re Asbestos Cases*, 847 F.2d 523 (9th Cir. 1988); *Miller v. Schweickart*, 413 F. Supp. 1062, 1068 (S.D.N.Y. 1976). As summarized below, Holmes' conduct meets and exceeds the "substantial factor" test.

[63] *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, *reh'g denied*, 423 U.S. 884 (1975).

[64] *Marbury Management, Inc. v. Kohn*, 629 F.2d 705, 718 (2d Cir.) (Meskill, J. dissenting), *cert. denied*, 449 U.S. 1011 (1980);

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The narrow "loss causation" principles that courts have imposed under Rule 10b-5,[65] however, are inapplicable in RICO cases.[66] The District Court below erroneously cited *Sperber v. Boesky*,[67] to support its finding that causation under RICO is, in substance, no different than "loss causation" under Section 10(b).[68] The Second Circuit in *Boesky* did not mention, much less discuss, the relationship between RICO causation and "loss causation" under Section 10(b). Instead, the Second Circuit simply stated

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Globus v. Law Research Serv., Inc., 418 F.2d 1276, 1292 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970).

[65] *E.G., Hatrock v. Edward D. Jones & Co.*, 750 F.2d 767, 773 (9th Cir. 1984).

[66] In *Bastian v. Petren Resources Corp.*, 699 F. Supp. 161 (N.D. Ill. 1988), the District Court speculated that "[w]hen the RICO violation is based upon a foundation of § 10(b) claims, *in most cases* the failure to prove loss causation under § 10(b) will result in a failure to prove proximate causation under § 1964(c) of RICO." *Id.* at 165 (emphasis added). Assuming *arguendo* the soundness of the dictum in *Bastian*, this case is unlike "most cases," including the simple misrepresentations made in *Bastian*. **This case involves an incredibly complex scheme to manipulate numerous securities by a variety of means over a long period of time by a large number of co-conspirators.** Further, plaintiffs' RICO claims are not based upon a "foundation of § 10(b) claims" but rather are based upon defendants' participation in a scheme of fraud in the sale of securities, wire fraud and mail fraud. Parenthetically, *Bastian* did not even address claims based on the predicate acts of wire and mail fraud.

[67] 849 F.2d 60 (2d Cir. 1988).

[68] Statement of Uncontroverted Facts and Conclusions of Law (Causation), C.R. 1342, p. 10 ¶ 23.

that "plaintiffs cannot show that their injuries were *proximately caused* either directly or indirectly by Boesky's racketeering violation."[69] The Second Circuit merely found that the injuries caused by the *Boesky* plaintiffs were too remote under traditional common law concepts of proximate cause. As such,*Boesky* supports the proposition that common law proximate cause is the measure here.[70]

The traditional common law of causation relating to intentional torts as applicable here is found in the Restatement (Second) of Torts at Section 435A which states:

> "A person who commits a tort against another for the purpose of causing a particular harm to the other is liable for such harm if it results, whether or not it is expectable, except where the harm results from an outside force the risk of which is not increased by the defendant's act."[71]

Under this doctrine, since Holmes participated in both the Bunnington and Aero Systems stock manipulations, as a part of the scheme shown below, the harm which

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[69] *Boesky*, 849 F.2d at 64 (emphasis added). *See Mead*, 523 F.2d at 1376); *Haroco, Inc.*, 747 F.2d at 398; *Brandenburg v. Seidel*, 859 F.2d 1179, 1189 (4th Cir. 1988). *See also Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. at 497 n.15 (approving recovery for both direct and ultimate harm flowing from defendant's conduct); *see* Section V.C.2 at pp. 46-49, *infra*.

[70] Accord Zervas v. Faulkner, 861 F.2d 823, 832-835 (5th Cir. 1988); *Brandenburg v. Seidel*, 859 F.2d 1179, 1187-1190 (4th Cir. 1988).

[71] The authors state that the rules of cause-in-fact for negligent conduct apply in the case of intentional conduct. Restatement 2d of Torts, § 870, comment 1.

resulted from those illegal acts – regardless of whether or not Holmes expected such harm – is Holmes' responsibility.[72]

2. The Court Found That There Was An Issue Of Material Fact Whether Holmes' Conduct Was The Proximate Cause Of Injury To SIPC And The Trustees.

The District Court found genuine issues of material fact concerning whether Holmes participated in a conspiracy[73] to violate RICO Sections 1962(a), 1962(b) and 1962(c), and that there was an issue present as to whether the alleged predicate acts, including fraud in the sale of securities, *caused* injury to SIPC and the Trustees.[74] Nevertheless, the District Court found that Holmes' conduct was not the "legal" or "proximate" cause of injury to the

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[72] Holmes will argue that even if he participated in the scheme (*i.e.*, intentionally invaded the legally protected interests of the Target Securities stockholders), SIPC is too remote to recover. In such a case, the Restatement (Second) of Torts at Section 435B, provides that Holmes' intent to commit the invasion, Holmes' degree of moral wrong in acting, and the seriousness of the harm which Holmes intended "are important factors in determining whether he is liable for resulting unintended harm." *See also Miller v. Schweickart*, 413 F.2d Supp. at 1068 (causation analysis examines "the extent to which the defendants" conduct created a continuous and active potential for harm").

[73] The conspiracy alleged in the First Amended Complaint, and in which the District Court found triable issues for purposes of these motions in composed of, *inter alia*, Holmes, Aero Systems, Lugo and Vigman. C.R. 1317, p. 1.

[74] Order Granting Summary Judgment (RICO claims) C.R. 1343, pp. 2-3, ¶¶ 5, 6, 8.

plaintiffs under RICO.[75] This determination is both irreconcilable as a matter of law with the District Court's RICO conspiracy finding and is, based on the evidence submitted, independently, patently and factually erroneous.

The law of conspiracy is so well-settled that it hardly needs citation; one is liable for the acts of a co-conspirator done in furthering a common plan, *i.e.*, all conspirators are liable for the acts of their co-conspirators.[76] Thus, since evidence of a conspiracy was found to exist, and three of the conspirators are Holmes, Lugo and Vigman,[77]

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[75] *Id.*; Order Granting Summary Judgment (Causation) C.R. 1344, pp. 1-2, ¶¶ 1-4. Even if the "loss causation" principles relied upon by courts under Section 10(b) were applied. Holmes is liable both as a direct participant and aider and abettor in the overall scheme to manipulate the Target Securities. *Kafton v. Baptist Park Nursing Center, Inc.*, 617 F. Supp. 349, 350-51 (D. Ariz. 1985) (In 10b-5 case "causal nexus is not between a particular misrepresentation and plaintiff's loss, but between the entire functioning scheme and the injury").

[76] *See e.g. Kashi v. Gratsos*, 790 F.2d 1050, 1054-1055 (2d Cir. 1986); *Beltz Travel Serv. Inc. v. Int'l Air Transp. Ass'n*, 620 F.2d 1360, 1367 (9th Cir. 1980). *See generally Nalle v. Oyster*, 230 U.S. 165, 182 (1913) common law civil conspiracy; well-settled rule injury from overt act actionable); *Halberstam v. Welch*, 705 F.2d 472, 487 (D.C. Cir. 1983) (conspiracy to commit burglary, death by overt act of coconspirator actionable); *Rice v. Janovich*, 109 Wash.2d 48, 49-52, 58-62, 64-67, 742 P.2d 1230, 1232, 1236-38, 1239-40 (1987) (injury from over act of co-conspirator, even if not predicate act, actionable).

[77] The Holmes, Lugo and Vigman relationship goes back to 1966 and 1967. C.R. 1317, pp. 9, 15. Vigman is Holmes' "confidante" and "financial advisor" and exerts substantial influence over Holmes to this day. *Id.* pp. 6-15; Lugo's relationship with Holmes and Vigman is extremely close. *Id.* pp. 15-17.

acts of either or both Lugo[78] and Vigman[79] in furtherance of the conspiracy place liability on Holmes as if those acts were his own.

The evidence of the acts of co-conspirator Lugo that contributed to the collapse is legion. Lugo sold Aero Systems stock at manipulated prices to purchase extensive holdings of Bunnington and Aerosonics stock that were declining in price due to selling by other market makers.[80] At the time of sales of Aero Systems stock by Lugo at FSSC, the cash flow into FSSC was the greatest in its history.[81] Lugo contributed to the Aero Systems manipulation by "leading the bid," a common manipulative technique, and by FSSC's dominance and control over the market in Aero Systems stock between April

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[78] Lugo was disciplined and suspended by the Securities Exchange Commission. C.R. 1317, pp. 15 & 24. He was also censured and fined by the NASD in a proceeding in which the NASD alleged that Lugo manipulated the price of Bunnington stock. *Id.* p. 28.

[79] All elements of a RICO violation are present in this case, including the perpetration of a pattern of racketeering activity over a 15 years time span. These predicate acts include acts resulting in the debarment of Vigman from association with any securities broker/dealers (C.R. 1317, pp. 16-17), spin-off transactions resulting in administrative findings that Vigman violated the Securities Act of 1933 and the Securities Exchange Act of 1934 (*Id.* p. 20), civil consent decrees against Vigman relating to securities later swapped for Aero Systems stock (*Id.* pp. 29-37) and Vigman's criminal conviction for securities fraud relating to transactions in warrants of Holmes' company, Aero Systems. *Id.* p. 11.

[80] C.R. 1310, p. 6.

[81] *Id.* at p. 8.

1979 and April 1981.[82] Lugo falsified FSSC's looks and records by posting FSSC's liabilities to incorrect accounts in order to avoid detection in cursory NASD examinations.[83] Lugo also "parked" hundreds of thousands of dollars in securities during April and May of 1981 to allow FSSC to remain in business,[84] thereby increasing profitability to Holmes, Vigman and others. As a key factor in the manipulations, Lugo used FSSC to dry up the market supply of the Target Stocks, which eventually led to FSSC's demise when excessive inventories of Bunnington and Aerosonics stock drove FSSC into liquidation.[85]

Further, the facts presented to the District Court show that co-conspirator Vigman committed acts in furtherance of the plan to manipulate Bunnington stock.[86] Vigman himself had a securities account at FSSC with Lugo.[87] When the manipulated price of Aero Systems stock was near its artificially inflated zenith, Vigman sold

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[82] *Id.* at p. 14.

[83] *Id.* at 22.

[84] *Id.* at p. 24.

[85] *Id.* at p. 19.

[86] Vigman was a major shareholder of Bunnington at different times during the long history of the scheme. C.R. 1317, p. 31, n.34. Further, Vigman, with Holmes and Aero Systems, engineered the complex DCS transaction in 1976 by which Bunnington obtained the only viable asset of Vigman's defunct company and by which Vigman exchanged worthless stock for thousands of valuable shares of Aero System stock. *Id.* pp. 28-42.

[87] C.R. 1310, pp. 18 & 50.

181,565 shares for $1,148,963.13 through Lugo at FSSC.[88] Many of the shares were restricted from sale; however, Holmes materially assisted Vigman in lifting those restrictions in order to enrich his co-conspirator.[89] Lugo did not pay Vigman for these transactions until weeks after they had taken place, thereby providing Lugo with an estimated $223,000 to $278,075 in interest-free money for FSSC's trading account – money used to buy up the ever increasing supply of Bunnington and Aerosonics stock.[90] Vigman's sales of Aero Systems stock were timed along with Holmes' false press releases to maximize the price of Aero Systems stock.[91] These factors, taken together, show that Holmes, Vigman and Lugo acted in concert to manipulate these Target Securities, to the ultimate detriment of FSSC, Sebag, SIPC and the investing public.

Thus, even ignoring the acts of Holmes himself, since he is a co-conspirator, he is, *as a matter of law*, responsible for the damages caused by the acts of his co-conspirators.[92]

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[88] *Id.* at p. 15.

[89] *Id.* at pp. 16-17.

[90] *Id.* at pp. 18-19.

[91] *Id.* at p. 15.

[92] In a vain attempt to bolster his case and claim that plaintiffs' damages were caused by an "intervening cause," the District Court accepted a Holmes finding that the net capital violations were caused by the brokerage firms' management." C.R. 1342, p. 5, ¶ 21. This finding erroneously isolates Holmes from the acts of his co-conspirators and ignores not only the District Court's finding of conspiracy but the substantial issues

(Continued on following page)

3. Holmes Was A Principal, Co-Conspirator, And Aider And Abettor In The Bunnington Stock Manipulation That Holmes Admits Was a Substantial Cause Of Plaintiffs' Loss.

Holmes not only concedes, but affirmatively asserts that the price of Bunnington stock was "artificially inflated," and that the large concentration of Bunnington and Aerosonics securities in the FSSC and Sebag inventory accounts was a "substantial cause of the demise of the brokerage houses."[93] Also, in adopting the fact findings prepared by Holmes, the District Court found, *inter alia*, that net capital deficiencies at FSSC and Sebag resulted from "undue concentration" of Bunnington and Aerosonics stock.[94] Indeed, the evidence shows that the "undue concentration" of Bunnington stock was a key part and a natural result of the manipulation of Bunnington stock.[95]

Thus, if there is evidence to go to a jury that Holmes participated in the Bunnington manipulation, Holmes is liable by virtue of his own findings and admissions for

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of fact of the conspiracy as well. Holmes and the District Court conceded that "managment" caused the loss; the jury must decide whether or not Holmes conspired with "management" to cause it.

[93] C.R. 1281, pp. 12-13 (citing the NASD report concerning the failures of FSSC and Sebag); C.R. 1326, p. 34. The evidentiary record also supports the finding that Bunnington stock was manipulated. C.R. 1309, pp. 17-18, ¶ 22.

[94] C.R. 1342, p. 5, ¶ 20.

[95] C.R. 1310, p. 34, ¶ 81; p. 39, ¶ 96; p. 40, ¶ 99; p. 41, ¶ 101.

the net capital deficiencies and consequent loss to plaintiffs.

The overwhelming evidence that must go to the jury is that Holmes did participate in, and provided substantial assistance to, Vigman, Lugo and other co-conspirators[96] in connection with the manipulation of Bunnington stock:

> (1) Holmes traded heavily in Bunnington stocks through both broker-dealer transactions and private placements with Bunnington, purchasing Bunnington stock in large blocks from FSSC while selling in small lots through other broker-dealers in sixty-six separate carefully timed transactions. Holmes' trading pattern had the effect of stimulating a demand interest for Bunnington by constricting the floating supply; selling in small lots expanded the supply gradually so as not to cause a dramatic decline in the price.[97] Holmes' active trading in Bunnington yielded virtually no individual profits, and thus was intended to influence the market demand for Bunnington, thereby assisting Lugo and Vigman in the manipulation of Bunnington stock;[98]

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[96] The Bunnington manipulation required substantial assistance from defendants Isadore Diamond, who is Vigman's brother-in-law and the Chairman of the Board of Bunnington (C.R. 1317, p. 34, n.38; pp. 36 & 37), and Gordon McNeil, the President of Bunnington. The evidence of the manipulative activities of Diamond and McNeil were not material to these motions and thus not before the District Court at the time of hearing.

[97] C.R. 1310, pp. 37-39, ¶¶ 90-96.

[98] *Id.* pp. 39-41, ¶¶ 97-101. The only *sale* of Bunnington made by Holmes through FSSC was the "parking" transaction. *Id.*, pp. 25-29, ¶¶ 48-63.

(2) Holmes' trading through Lugo at FSSC dominated and controlled the market in Bunnington, a classic element of stock manipulation;[99]

(3) As of late April 1981, FSSC has a small, undetected net capital deficiency.[100] In order to obtain artificial compliance with SEC net capital regulations, defendant Lugo falsified the books and records of FSSC by, *inter alia*, "parking" significant volumes of FSSC inventory stocks such as Bunnington in customer accounts, including Holmes' account.[101]

On May 20, 1981, a purchase order for 5,000 shares of Bunnington stock was entered in Holmes' account.[102] The transaction "parked" shares in Holmes' account in order to artificially increase FSSC's net capital.[103] This parking transaction was significant not only because it was a riskless transaction for Holmes,[104] who did not pay for the shares, but because it reveals Holmes' complicity, participation and cooperation in keeping the manipulation scheme together at a time of crisis.

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[99] *Id.* pp. 39-40, ¶¶ 97-99; C.R. 1317, p. 94.

[100] C.R. 1310, p. 21, ¶¶ 34-35.

[101] *Id.* pp. 21-22, ¶¶ 37-38; pp. 23-29, ¶¶ 43-63. By placing FSSC inventory stocks in customer accounts, FSSC reduced the minimum net capital requirements imposed by SEC regulations. Inventory stocks, unlike customer account stocks, are discounted in value in order to assess net capital compliance. This discount is commonly referred to as a "haircut", *Id.* p. 20, ¶ 32 n.7.

[102] *Id.* p. 25, ¶ 49.

[103] *Id.* pp. 25-30, ¶¶ 48-63.

[104] *Id.* p. 26, ¶ 53.

The parking of stocks at FSSC did not merely mask existing damage, as the District Court found,[105] but created dramatic independent losses to FSSC.[106] By parking large volumes of securities in April and May of 1981, Lugo was able to conceal FSSC's net capital deficiency and continue to operate the firm until July 24, 1981.[107] The increased losses associated with the scheme to conceal FSSC's net capital deficiency were estimated conservatively at $1,855,382.[108]

(4) The *modus operandi* of publishing false and misleading information to public investors was utilized regularly by Holmes and the other defendants.[109] In May of 1981, Holmes participated directly in the Bunnington manipulation when Bunnington issued one of its many false and misleading press releases, and Holmes published it as fact by wire directly to Moore Schley

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[105] C.R. 1342, p. 7, ¶ 35.

[106] C.R. 1310, p. 24, ¶ 45.

[107] *Id.* p. 24, ¶ 47; pp. 34-35, ¶ 81.

[108] When the price of Target Security Bunnington plummeted in late July 1981 from approximately $11 per share to $2.50 per share, FSSC could no longer mask the net capital deficiency that had been growing since April 1981 and the brokerage house collapsed. Moreover, the failed efforts by Holmes, Lugo, Vigman and other co-conspirators to perpetuate the manipulation of FSSC through July 1981 toppled Sebag as well. As of May 29, 1981, Sebag carried only $110,000 of its inventory in manipulated stocks Aerosonics, Bunnington, Dash and Osrow. C.R. 1310, p.30, ¶ 64. Thereafter, through Lugo's transfers to Sebag, Sebag increased its inventory in those stocks by more than $7 million, forcing the firm into liquidation on July 27, 1981. *Id.* pp. 30-31. ¶¶ 65-68.

[109] *See e.g.*, C.R. 1317, pp. 58-83; pp. 95-97; pp. 104-105.

Cameron & Company ("Moore Schley"),[110] a broker/dealer in New York.[111]

(5) Holmes personally promoted Bunnington stock through Moore Schley, introduced Moore Schley to Bunnington principals who sold Bunnington stock through Moore Schley and discussed the availability of financing for Bunnington with Moore Schley;[112]

(6) Holmes tried to support the price of Bunnington stock even after the collapse of FSSC and Sebag. One week after the collapse he borrowed $600,000 to support additional Bunnington purchases and secured the loan with 528,000 shares of manipulated Aero Systems stock;[113] and

(7) Holmes profited from insider information from Bunnington.[114]

Holmes had a compelling motive to artificially prop up Bunnington's price: greed. For $100,000 in September of 1979, Holmes bought a Bunnington debenture convertible into 40,000 shares of Bunnington common stock (*i.e.* for $2.50 per share).[115] After the two year holding period the restricted stock would have become unrestricted and saleable on the open market (*i.e.* in September 1981). About the time he bought the convertible debenture,

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[110] Moore Schley was also the broker-dealer who actively assisted Holmes in the successful unlawful manipulation of Holmes' Aero Systems stock. C.R. 1317, pp. 71-81.

[111] *Id.* p. 71.

[112] *Id.* pp. 95-97.

[113] *Id.* p. 98.

[114] *Id.* pp. 95-97.

[115] *Id.* p. 92.

Holmes began trading Bunnington in a manner that contributed to the manipulated price rise of Bunnington stock.[116] Holmes also touted Bunnington stock,[117] published a false laudatory press release about Bunnington,[118] and parked Bunnington stock with Lugo at FSSC.[119] During this period (August 1979 through July 1981), Bunnington stock rose from approximately $3.50 per share to $12.25 per share.[120] All Holmes had to do was keep the price up for two more months (*i.e.* from July through September) and his 40,000 shares would be worth approximately one- half million dollars. Despite all of his efforts, and those of his co-conspirators Lugo and Vigman, Holmes did not quite make it.[121]

Of course, Holmes will vociferously deny all of the above, and will provide numerous excuses. But he has admitted – at least for purposes of his motions, and this

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[116] C.R. 1310, pp. 37-39, ¶¶ 90-96; C.R. 1296, Ex. 3863.

[117] C.R. 1317, pp. 95-97.

[118] *Id.* p. 96.

[119] C.R. 1310, pp. 25-29, ¶¶ 48-63.

[120] C.R. 1296, Ex. 3863.

[121] On July 24, 1981, FSSC held 62,043 shares of Bunnington at an average cost of $11.0456 per share. By reason of a sudden deflation in the price of Bunnington, the market value of those shares on the date the liquidation proceeding commenced was $2.50 per share. C.R. 1310, p. 36, ¶ 88. On July 27, 1981, Sebag held 73,640 shares of Bunnington at an average cost of $10.89 per share. The Market value of the shares on the date the liquidation proceeding commenced was $2.50 per share (*Id.* p. 32, ¶¶ 72-73). Thus, the total trading losses to FSSC and Sebag in Bunnington alone were approximately $1.15 million.

Court must accept as a fact – that *the Bunnington manipulation was a substantial contributing factor* to the injuries to the plaintiffs; and if Holmes did what plaintiffs say he did, Holmes caused the loss, or at least it must be for jury to say that he did not. Under these facts, a court simply cannot decide that Holmes is not liable to plaintiffs as a matter of law.

4. The Manipulation Of Aero Systems Stock By Holmes And His Co-Conspirators Was The Linchpin Of The Scheme To Manipulate Bunnington And Aerosonics Stocks.

Apparently, the District Court viewed Holmes' manipulation of Aero Systems stock as an isolated event and erroneously accepted his argument that that manipulation had "no impact" on the net capital deficiencies;[122] *i.e.*, the Court considered Holmes' primary role in the Aero Systems manipulation in isolation.[123] The law,

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[122] C.R. 1342, p. 5, ¶ 22. Holmes also argued, and the Court accepted, that because the brokerage houses' inventories of Aero Systems stock were not material, Holmes' Aero Systems manipulative activities did not contribute to the collapse of FSSC and Sebag. *Id.* p. 8, ¶ 7.

[123] Holmes conceded for purposes of the motion that he participated in the manipulation of Aero Systems securities. C.R. 1281, p. 11. As well he should; it is difficult to see how a trier of fact could find otherwise in light of the literally overwhelming evidence of Holmes' carefully calculated and intense "hyping" of the stock and the "CD-3000," Aero Systems' so-called "fuel savings" device. C.R. 1317, pp. 42-83. Characteristically, his misrepresentations to the public continued when, after the summary judgments were granted on the narrow legal grounds herein, and despite the District Court's clear

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however, is indisputable " . . . that 'a conspiracy [is] not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole.' "[124] The Court failed to consider what part Holmes' manipulation of Aero Systems had in the entire scheme.[125]

The manipulation of Aero Systems stock was critical to the excess inventory build-up in Bunnington and Aerosonics stocks at Sebag,[126] and thus the scheme to manipulate and falsely inflate the Bunnington stock (as well as

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findings of fact that Holmes' conduct was sufficiently questionable that it should go to a jury, Holmes issued a press release to his stock buying public on November 2, 1988, stating that he had been "vindicated". C.R. 1364, Ex. "A". Incredibly, Holmes also has threatened plaintiffs with an action for malicious prosecution despite the overwhelming evidence of Holmes' participation in, and engineering of, the fraudulent schemes. C.R. 1364, Ex. "C".

[124] *Beltz*, 620 F.2d at 1366, citing *United States v. Patten*, 226 U.S. 525, 544 (1913).

[125] Holmes contends that the manipulation of Aero Systems securities satisfies the "but for" causation requirement but fails to support "loss causation." C.R. 1326, p. 27. However, as shown above, loss causation principles do not apply to RICO claims such as this. *See supra*, n.66. Further, the manipulation of Aero Systems securities directly funded and manipulation of Bunnington and other Target Securities. C.R. 1310, p. 33, ¶¶ 76-79. Each manipulation was part of a scheme, not unrelated acts separated by intervening forces as Holmes would conveniently assert.

[126] Holmes' role in the manipulation of Aero Systems stock allowed Sebag to obtain substantial loans from First Interstate Bank which were used to acquire large inventory positions in Bunnington and Aerosonics securities. *Id.*

the others). By April 24, 1981, when FSSC first experienced a net capital deficiency, the manipulation of Aero Systems had succeeded.[127] In April and May of 1981, Holmes' "financial advisor" and co-conspirator Vigman sold massive volumes of inflated Aero Systems stock to FSSC for proceeds of $1,148,963.[128] Lugo immediately resold the Aero Systems stock and then delayed payment to Vigman, thereby allowing FSSC with those funds to acquire large inventory positions in Bunnington, Aerosonics and Creditbank securities.[129] As a direct result of Holmes' manipulation of Aero Systems stock and the April-May 1981 sales of Aero Systems at inflated prices from Vigman to Lugo to the public, Lugo was able to purchase the substantial volumes of these other Target Securities.[130] The inventory increase, predominantly in Bunnington and Aerosonics stock was necessary to maintain those stocks' prices at the artificially inflated level, since considerable sell pressure was experienced at that time. As Holmes admits, the escalation of inventory led to the demise of FSSC and Sebag.[131]

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[127] C.R. 1310, p. 21. Holmes' media campaign to inflate the price of Aero Systems stock resulted in a price increase in excess of 137% from September 1980 through May 1981, C.R. 1309, p. 14, ¶ 15.

[128] C.R. 1310, p. 18, ¶ 26.

[129] *Id.* pp. 17-19, ¶¶ 24-29.

[130] *Id.* p. 19, ¶ 30. When FSSC acquired substantial positions in Bunnington, Aerosonics and Creditbank, the book value of FSSC's inventory exceeded its capitalization by more than 300%. *Id.* p. 19, ¶ 30.

[131] C.R. 1281, pp. 12-13.

Thus, the evidence shows beyond doubt that it is a jury question with respect to the effect of Holmes' manipulation of the Aero Systems stock in furtherance of the scheme to manipulate the market prices of Bunnington and Aerosonics stock (which, as Holmes admits, caused the collapse of the brokerage houses).[132]

C. The District Court Erred In Granting Summary Judgment To Holmes When It Held That SIPC Must Be A "Purchaser Or Seller" Of Securities To Maintain An Action Under 18 U.S.C. Section 1964(c) For Conduct Consisting Of (a) "Any offense . . . Involving Fraud In The Sale Of Securities . . . Punishable Under Any Law Of The United States," (b) Wire Fraud Or (c) Mail Fraud In Violation Of 18 U.S.C. Section 1962.

1. Application Of RICO: No Purchaser/Seller Limitation.

Interpretation of RICO begins with its text,[133] and structure as well as language is important.[134] The various ways that RICO's substantive standards may be violated each requires a "pattern of racketeering activity."[135] 18

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[132] In "cases of this kind, it is for the jury, as trier of fact, to determine the question of causation." *Costner v. Blount Nat'l Bank of Maryville*, 587 F.2d 1192, 1195 (6th Cir. 1978) (multiple factors in conflict under Bank Holding Company Act).

[133] *H.J., Inc.*, 57 U.S.L.W. at 4953; *United States v. Monsanto*, 57 U.S.L.W. 4826, 4827 (June 22, 1989); *Russello*, 464 U.S. at 20 (citing *Turkette*, 452 U.S. at 587).

[134] *Russello*, 464 U.S. at 22-23; *United States v. Turkette*, 452 U.S. at 582; 587.

[135] 18 U.S.C. §1962(a)-(d). *Jarvis v. Regan*, 833 F.2d 149, 152 (9th Cir. 1987) *cert. denied*, 108 S. Ct. 2851 (1988) ("common thread").

U.S.C. Section 1961(1), which includes RICO's predicate acts, defines "racketeering activity" to mean:

> "(B) any act . . . under . . . title 18 . . . section 1341 (relating to mail fraud), section 1343 (relating to wire fraud) . . . "
>
> • • •
>
> "(D) any offense involving . . . fraud in the sale of securities . . . punishable under any law of the United States. . . . "

These substantive standards are enforced through 18 U.S.C. Sections 1963 (criminal) and 1964 (civil). Section 1964 defines who may sue ("any person") and who may be sued ("any person"), what the person may sue for (injury "to business or property"), and when such injury is compensable ("by reason of a violation"). RICO, therefore, is explicit and comprehensive in its articulation of its substantive standards and the structure of its remedial framework.

a. The Language Of 18 U.S.C. Section 1964(c) Is Not Limited By A Purchaser/Seller Requirement.

Section 1962 is enforced by private suits through 18 U.S.C. Section 1964(c), which provides that "[a]ny person injured in his business or property by reason of a violation of section 1962" may sue. The definition of "person" includes "any individual or entity capable of holding a legal or beneficial interest in property."[136] The plain text of RICO does not impose "purchaser or seller" limitations

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[136] 18 U.S.C. § 1961(3).

on "any person."[137] Had Congress wanted to narrow the class of persons entitled to sue to enforce RICO's remedial provisions, it could have narrowed the definition of "person" in this section; Congress could have "narrowed the sweep of the definition by inserting a single word".[138] " 'The short answer [to the contention that RICO is limited by purchaser-seller limitations] is that Congress did not write the statute that way.' "[139]

Therefore, it was improper for the District Court to read into the statute a "purchaser or seller" limitation that the courts have implied for private civil actions arising under Section 10(b) and Rule 10b-5 of the Exchange Act.[140]

Congress explicitly set out the only limitations on civil recovery under RICO. The "person" must show that "his business or property" was "injured."[141] "In addition,

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[137] *Bankers Trust Co. v. Rhoades*, 859 F.2d 1096, 1099 (2d Cir. 1988), *cert. denied*, 109 S. Ct. 1642 (1989) ("no special limitation on standing").

[138] *See Turkette*, 452 U.S. at 581 (definition of "enterprise").

[139] *Monsanto*, 57 U.S.L.W. at 4829 ("any property" does not exclude funds for legal fees) (quoting *United States v. Naftalin*, 441 U.S. 768, 773 (1979)).

[140] *Compare H.J., Inc.*, 57 U.S.L.W. at 4954-4956 ("pattern" not limited to organized-crime-type perpetrator); *Sedima*, 473 U.S. at 495 ("any person" not limited to "mobsters"); *Russello*, 464 U.S. at 21-22 ("any interest" not limited to "interest in enterprise"); *Turkette*, 452 U.S. at 580-81 ("any enterprise" not limited to "illegal enterprise"); *Lou v. Belzberg*, 834 F.2d at 736 ("exclusive" may not be read into Section 1964(c)).

[141] *First Pac. Bancorp. Inc. v. BRO*, 847 F.2d 542, 547 (9th Cir. 1988).

the plaintiff only has standing if, and can only recover to the extent that, he has been injured in his business or property by the conduct constituting the violation. . . . But the statute requires no more than this."[142]

b. "Fraud In The Sale Of Securities" Under RICO Does Not Include Purchaser/Seller Limitations.

Since the judiciary implied a private claim for relief in Rule 10b-5, circumscribing it by an implied standing rule may be appropriate.[143] However, the private right of action under Civil RICO is *express*, and a judicial limitation on its scope by implied standing rules is improper. To require Civil RICO plaintiffs to be purchasers or sellers ignores the clear teaching of *Blue Chip Stamps:* the "[j]udiciary may not circumscribe [an express claim for relief] . . . because of any disagreement it might have with Congress about the wisdom of creating so expansive a liability."[144] *H.J., Inc.'s* and *Monsanto's* teachings are also relevant here: "RICO's language supplies no ground to believe that Congress meant to impose such a limit on the Act's scope."[145] "[T]he statute, as presently written, cannot be read any other way."[146] *Sedima*, too, is

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[142] *Sedima*, 473 U.S. at 496-497; *see Marshall & Ilsley Trust Co. v. Pate*, 819 F.2d at 807 ("wrong to require a plaintiff to show" more).

[143] *Blue Chip Stamps*, 421 U.S. at 749.

[144] *Id.* at 748.

[145] *H.J., Inc.*, 57 U.S.L.W. at 4955 ("pattern" not limited by organized crime).

[146] *Monsanto*, 57 U.S.L.W. at 4829 ("any property" does not exclude funds for legal fees).

unequivocal: liability under RICO must not be judicially limited: "it is a form of statutory amendment [in] appropriately undertaken by the courts."[147] "[C]orrection must lie with Congress," if it is "a defect."[148] "[R]ewriting . . . [RICO] is a job for Congress, if it is so inclined, and not for [a court]."[149]

Accordingly, "any offense . . . involving fraud in the sale of securities . . . punishable under any law of the United States," the operative RICO provision, is not limited by "purchaser or seller" standing requirements.[150]

Although the plain language of RICO and the Supreme Court's teaching preclude judicially imposed limitations on standing under RICO, some courts nevertheless impose artificial standing requirements on the statute. *International Data Bank, Ltd. v. Zepkin*[151] is the principal decision in opposition. The Fourth Circuit in *Zepkin* concedes that Congress did not *expressly* limit RICO by "purchaser or seller" limitations, noting the absence not only of "purchaser-seller" language but also of Section 10(b)'s "in connection with" causation standard. Yet the *Zepkin* court argued that explicit statutory

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[147] *Sedima*, 473 U.S. at 500 (injury not limited to racketeering type).

[148] *Id.* at 499.

[149] *H.J., Inc.*, 57 U.S.L.W. at 4956.

[150] *Warner v. Alexander Grant & Co.* 828 F.2d 1528, 1530 (11th Cir. 1987) ("The federal RICO statute has no requirements analogous to the 'purchase or sale' requirement of the federal securities law.").

[151] 812 F.2d 149 (4th Cir. 1987), *cert. denied*, 108 S. Ct. 698 (1988).

language was required in RICO to overcome judicially imposed limitations on private actions under Rule 10b-5.[152] *Zepkin* is fundamentally misguided, misreads the statutory scheme of RICO, and reflects bad policy.[153]

First, *H.J., Inc., Monsanto,* and *Sedima* squarely hold that RICO's express text structure and legislative history, not its silence in the text or legislative history, control the interpretation of RICO.[154] RICO must be liberally construed, and its remedial purpose is to be enhanced, not retarded.[155] The Fourth Circuit ignores the implications of the liberal construction clause for its narrow interpretation of the statute. Indeed, *Zepkin* does not even address 18 U.S.C. Section 1964, the civil provision that, in fact, *expressly* deals with standing, injury, and causation. As *Sedima* noted, moreover, it was expressly to avoid such narrow standing limitations on RICO's remedies that the legislation was enacted outside of the antitrust statutes.[156] By reading such limitations back into RICO, the Fourth Circuit "create[s] exactly the problems Congress sought to avoid."[157]

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[152] *Zepkin*, 812 F.2d at 152.

[153] *See Federenko v. United States*, 449 U.S. 490, 513 (1981) (A court is "not at liberty to imply . . . a condition which is opposed to the explicit terms of the statute . . . To [so] hold . . . is not to construe the Act but to amend it.") (quoting *Detroit Trust Co. v. The Thomas Barlum*, 293 U.S. 21, 38 (1934)).

[154] *H.J., Inc.* 57 U.S.L.W. 4951 at 4953; *Monsanto*, 57 U.S.L.W. 4826 at 4827-4829; *Sedima*, 473 U.S. at 495 n.13.

[155] *Sedima*, 473 U.S. at 497-498.

[156] *Id.* at 498.

[157] *Id.* at 499. Some overlap between statutes "is neither unusual nor unfortunate." *S.E.C. v. Nat'l Secs.*, 393 U.S. 453, 468

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Rule 10b-5 standing limitations are inapplicable to RICO on another more fundamental ground. By itself, the implied claim for relief of Rule 10b-5 seeks only private *civil* redress. RICO, however, seeks to make effective the substantive standards of the statute through both criminal and civil sanctions. The substantive standards of RICO reflect the substantive elements of its predicate acts, each of which is crime. RICO fills this objective civilly through a private attorney general enforcement mechanism.[158] The purchaser/seller limitation of Rule 10b-5 is imposed only for private civil actions. The violation of Rule 10b-5 that constitutes a predicate act under RICO, however, is a *criminal* securities fraud. "Offense . . . punishable" "obviously refers to [the] criminal" provisions of the securities statutes.[159]

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(1969). Indeed, the securities statutes themselves envision it. *See e.g.*, 15 U.S.C. § 78bb (a)("rights and remedies . . . in addition" to "any and all other rights" that exist).

[158] *Agency Holding Corp.*, 483 U.S. at 151; *Shearson/American Express Inc.*, 482 U.S. at 241; *Sedima*, 473 U.S. at 493.

[159] *Trane Co. v. O'Connor Secs.*, 718 F.2d 26, 29 (2d Cir. 1983). *See* Section 32(a) of the Securities Exchange Act of 1934, 84 Stat. 904 ("willfully violates"). The standards of Section 32(a) are not limited by "purchaser-seller" limitations. *United States v. Charmay*, 537 F.2d 341, 349 n.11 (9th Cir.) *cert. denied* 429 U.S. 1000 (1976). ("In a criminal prosecution, the standing problem is, of course, not present and Rule 10b-5 is applicable if the conduct charged falls within the Rule's prohibition."). *See also United States v. Naftalin*, 441 U.S. 768, 774 n.6 (1979) (*Blue Chip Stamps* does not limit criminal provisions); *United States v. Newman*, 664 F.2d 12, 17 (2d Cir. 1981), *cert. denied*, 464 U.S. 863

(Continued on following page)

Plaintiffs under RICO, especially public benefit corporations such as SIPC, act as private prosecutors.[160] Had Congress wanted to impose "purchaser-seller" standing limitations on this civil enforcement mechanism, it could have done so with appropriate language. Congress was well-aware of the overlap between RICO and the securities statutes, as the point was specifically drawn to its attention.[161]

Forcing Civil RICO into a purely private law model, as the Fourth Circuit does in *Zepkin*, misconceives Civil RICO's important *public* law functions.[162]

c. Mail And Wire Fraud Do Not Include Purchaser/ Seller Limitations.

No language in the mail or wire fraud statutes warrants reading into them "purchaser or seller" limitations.

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(1983) ("It is only because the judiciary . . . created a private cause of action . . . that standing . . . has become a pivotal issue").

[160] *See Lou v. Belzberg*, 834 F.2d at 739 ("encourage enforcement of RICO").

[161] *Civil Action*, 68 Notre Dame L. Rev. at 272-73. Cumulative remedies enhance remedial purposes. *Herman & McLean v. Huddleston*, 459 U.S. 375, 386 (1983).

[162] *See generally* Chayes, *Foreword: Public Law Litigation and The Burger Court*, 96 Harv. L. Rev. 4-5 (1982) (classic model of private dispute resolution contrasted with contemporary model of public grievances against aggregates of power); *Id.* at 8-26 (inappropriate private law standing limitations analyzed); Chayes, *The Role of the Judge in Public Law Litigation*, 89 Harv. L. Rev. 1281 (1976).

The purpose of the two statutes, taken together, is to prohibit schemes to defraud that utilize, in varying circumstances, the mails or interstate wire communications.[163] The statutes say nothing about "purchasers or sellers."

Only two elements need come together: a scheme to defraud and the use of the mails or interstate wires to execute it.[164] A "scheme to defraud" is not limited to common law concepts of fraud.[165]

Conceptual difficulties may arise, however, when parties or courts "confus[e] mail fraud with common law fraud,"[166] since (1) neither "purchaser or seller" standing limitations, (2) materiality or justifiable and detrimental reliance, nor (3) misrepresentation or omission are elements that circumscribe the substantive definition of a "scheme to defraud" in the mail and wire fraud statutes

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[163] *Parr v. United States*, 363 U.S. 370, 389 (1960); *United States v. Bohonus*, 628 F.2d 1167, 1171 n.7 (9th Cir.), *cert. denied*, 447 U.S. 928 (1980) (mail and wire fraud read together).

[164] *Pereira v. United States*, 347 U.S. 1, 8-9 (1954); *Sun Sav. & Loan Ass'n v. Dierdorff*, 825 F.2d 187, 195 (9th Cir. 1987).

[165] *Durland v. United States*, 161 U.S. 306, 314 (1896). *See generally Bohonus*, 628 F.2d at 1171 ("non-technical standard") (citing *United States v. Louderman*, 576 F.2d 1383, 1389 (9th Cir. 1978), *cert. denied*, 439 U.S. 896 (1978)); *Dennis v. United States*, 384 U.S. 855, 860-861 (1966); *Hammerschmidt v. United States*, 265 U.S. 182, 188 (1924); *Haas v. Henkel*, 216 U.S. 462, 478-480 (1910); *Equitable Relief*, 62 Notre Dame L. Rev. at 587-588 n.237; Rakoff, *The Federal Mail Fraud Statute*, 18 Duq. L. Rev. 771 (1980) (general treatment of development of mail fraud).

[166] *Armco Indus. Credit Corp v. SLT Warehouse Co.*, 782 F.2d 475, 481 (5th Cir. 1986).

incorporated into RICO.[167] Accordingly, neither mail nor wire fraud's concepts of "scheme to defraud" under RICO are limited by "purchaser or seller" standing or similar common law requirements. As such, the District Court's summary judgment cannot be legally justified.

2. The District Court Misread And Misapplied Standing Under RICO.

Standing under RICO is granted to "[a]ny person injured in his business or property by reason of *a violation of Section 1962.*"[168] Thus, a RICO plaintiff need not be injured by the predicate acts enumerated in Section 1961(1) to sue for a violation of Section 1962(a)-(d). Injury by any element of the violation, including an overt act under Section 1962(d), sufficies.

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[167] *Brandenburg v. Seidel*, 859 F.2d 1179, 1187 (4th Cir. 1988) (no detrimental reliance for mail or wire fraud); *Abell v. Potomac Ins. Co.*, 858 F.2d 1104, 1129 (5th Cir.), *reh'g denied*, 863 F.2d 882 (1988) (no materiality or reliance for mail or wire fraud); *Warner*, 828 F.2d at 1530 (no purchaser or seller standing limitations); *Armco Indus. Credit Corp.*, 782 F.2d at 481-82 (no justifiable or detrimental reliance for mail fraud); *McLendon v. Continental Group, Inc.*, 602 F. Supp. 1492, 1506-10 (D.N.J. 1985) (RICO scheme to defraud: noting inapplicability of misrepresentation or omission in "scheme to defraud"). *Cf. Wilcox v. First Interstate Bank of Oregon*, 815 F.2d 522, 531 n.7 (9th Cir. 1987) ("need not decide" if elements of common law fraud and RICO mail fraud identical; *Armco* noted); *United States v. Halbert*, 640 F.2d 1000, 1007-09 (9th Cir. 1981) (no misrepresentation required, but if alleged, materiality, but not reliance, necessary.)

[168] 18 U.S.C. § 1964(c) (emphasis added).

In *Sedima*, the United States Supreme Court squarely addressed the issue of whether injury solely caused by predicate acts is sufficient to give standing. The defendants contended that only injury caused by the entire violation was cognizable. The Court did not restrict standing under RICO to those injured only by predicate acts. On the contrary, the Court *expanded* standing for those suing under Section 1962(c) to *include* plaintiffs only injured by predicate acts, because "the essence of the violation is the commission of those acts in connection with the conduct of an enterprise."[169]

Footnote 15 of the majority opinion in *Sedima* expressly recognized that recovery for those "injured . . . by reason of a violation of Section 1962" also *includes* those injured by the completed RICO violation itself. The Court stated:

> "Any recoverable damages occurring by reason of a violation of § 1962(c) will flow from the commission of the predicate acts.[15] . . .
>
> "[15]Such damages include, but are not limited to, the sort of competitive injury for which the dissenters would allow recovery."[170]

Unfortunately, the District Court here did not issue a written opinion explaining its rationale concerning its decision. But, apparently, the District Court has misread the standing rule of *Sedima* to require injury caused *only* by the predicate act of fraud in the sale of securities,

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[169] *Sedima*, 473 U.S. at 497 & n.15.

[170] *Id.*

because the District Court ignored the overwhelming evidence of Holmes' participation in the Bunnington manipulation and the key role that Holmes' manipulation of Aero Systems played in it. Instead, the District Court focused *solely* on the Aero Systems manipulation, concluded it had ended, and because SIPC was not a "purchaser or seller" of Aero Systems, concluded that SIPC had no standing to bring suit. The substance of the District Court's holding is that the only predicate act about which SIPC can complain is a Rule 10b-5 violation and that only Rule 10b-5 violations (predicate acts) violate RICO. This holding completely ignores the clear dictate of Congress that persons injured "by reason of *a violation of Section 1962*"[171] may seek redress for their injuries. The District Court's interpretation of Section 1964(c) is not warranted, as a plain reading of the statute reveals; nor can such an artificial rule that standing is *only* granted to those injured by predicate acts withstand a careful review of *Sedima*.

That the plaintiffs have been injured as a result of a violation of Section 1962 is clearly shown and supported by Holmes' investment of proceeds from the sale of one manipulated security into another. Section 1962(a) makes it unlawful to obtain an interest in an enterprise by investing or using in it income derived from a pattern of racketeering.[172] SIPC alleged and presented genuine issues of material fact that Holmes violated Section

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[171] U.S.C. § 1964(c) (emphasis added).

[172] 18 U.S.C. § 1962(a).

1962(a), and that SIPC has standing to sue for that violation. Such genuine issues are supported by the uncontroverted fact that Holmes invested income derived from a pattern of racketeering activity, the manipulation of Aero Systems stock, into an enterprise, Bunnington Corporation.[173] This investment into the enterprise, perpetrated to further the Bunnington manipulation,[174] injured SIPC in its business when the broker-dealers failed. Thus, SIPC has standing by virtue of the violation of Section 1962(a) of RICO itself to recover damages resulting from this investment. These rights exist under Sections 1962(a) and 1964(c), *regardless* of whether SIPC has standing to sue as a "purchaser or seller" of securities under Section 10(b).

VI

CONCLUSION

For the foregoing reasons, SIPC and the Trustees must be allowed to try their cases against defendant Holmes.

DATED: August 1, 1989

STEPHEN C. TAYLOR
JOSEPH F. COYNE, JR.
JOEL E. BONNER
SHEPPARD, MULLIN, RICHTER & HAMPTON
G. ROBERT BLAKEY
CORNWELL & BLAKEY
Attorneys for Plaintiff-Appellant Securities Investor Protection Corporation

---

[173] C.R. 1310, pp. 45-49, ¶¶114-119.

[174] *Id.*

C. Edward Simpson
Michael J. Abbott
Jones, Bell, Simpson & Abbott
Attorneys for Plaintiffs-Appellants
Eugene W. Bell,
Trustee for the Liquidation of
Joseph Sebag Incorporated and
Laurence A. Schroeder,
Successor Trustee for the
Liquidation of First State
Securities Corporation

STATEMENT OF RELATED CASES
(Circuit Rule 28-2.6)

The following cases are hereby identified as "related cases":

1. *Securities Investor Protection Corp., et al. v. Vigman, et al.*, 764 F.2d 1309 (9th Cir. 1985), Docket Nos. 84-6074 and 84-6311. This case has previously been heard in this Court and involves the same transactions and events.

2. *Securities Investor Protection Corp. v. Vigman, et al.*, 803 F.2d 1513 (9th Cir. 1986), Docket No. 85-5786. This case has previously been heard in this Court and involves the same transactions and events.

PROOF OF SERVICE BY MAIL

STATE OF CALIFORNIA)
) ss.:
COUNTY OF LOS ANGELES)

I am a citizen of the United States and a resident of or employed in the City of Los Angeles, County of Los Angeles; I am over the age of 18 years and not a party to

the within action; my business address is 1706 Maple Avenue, Los Angeles, California 90015.

On August 1, 1989, I served the within Plaintiffs-Appellants' Opening Brief in re: "Securities Investor Protection Corporation vs. Robert G. Holmes, Jr." in the United States Court of Appeals for the Ninth Circuit, Nos. 89-55094 and 89-55128, and Excerpt of Record thereto, on all parties interested in said action, by placing two true copies thereof enclosed in a sealed envelope, with postage thereon fully prepaid, in the United States Post Office mail box at Los Angeles, California, addressed as follows:

Jack I. Samet, Esquire
David H. Bramson, Esquire
Julie B. Haupt, Attorney at Law
Buchalter, Nemer, Fields & Younger
700 South Flower Street
Suite 700
Los Angeles, California 90017

Counsel for Defendant:
Robert G. Holmes, Jr.

Michael A. Oswald, Esquire
Oswald & Yap
5000 Birch Street
Suite 4600
Newport Beach, California 92660

Counsel for Defendants:
Frankie Mae Garrity,
Rodger W. Garrity and
Velma Shaw (aka Velma Shaw Meyers)

Hugh Steven Wilson, Esquire
G. Andrew Lundberg, Esquire
Latham & Watkins
555 South Flower Street
Los Angeles, California 90071

Counsel for Defendants:
Gordon H. McNeil and Isadore Diamond

James W. Mercer, Esquire
Jeanne E. Irving, Attorney at Law
Hennigan & Mercer
611 West Sixth Street
28th Floor
Los Angeles, California 90017

Counsel for Defendants:
Magnetic Technologies Corp.
(Bunnington Corp.)

David L. Ross, Esquire
Greenberg, Traurig, Askew, Hoffman,
Lipoff, Rosen & Quentel
1221 Brickell Avenue
19th Floor
Miami, Florida 33131

Counsel for Defendant: Creditbank

Martin N. Gelfand, Esquire
Hochman, Salkin & DeRoy
9100 Wilshire Boulevard
7th Floor
West Tower
Beverly Hills, California 90212

Counsel for Defendants:
Nettie Vigman and Seymour Vigman

Steven Gourley, Esquire
Feinstin, Gourley & Mandel
11111 West Olympic Boulevard
Suite 300
Los Angeles, California 90064

Counsel for Defendants:
Jack Haber, Haberico, Inc.,
Habers, Inc. and Habers, Inc.,
a Defined Benefit Pension Trust

Steven P. Rice, Esquire
Kindel & Anderson
555 South Flower Street
29th Floor
Los Angeles, California 90071

Counsel for Defendant:
Aero Systems, Inc.

Lee Huszagh, Esquire
330 Alhambra Circle
Coral Gables, Florida 33134

Co-Counsel for Defendant:
Aero Systems, Inc.

Stephen H. Marcus, Esquire
Frandzel & Share
8383 Wilshire Boulevard
Suite 400
Beverly Hills, California 90211

Counsel for Defendants:
Dash Industries, Inc.
Jay Dash and Phillip Dash

William E. Taylor, III, Esquire
Leonard Dubin, Esquire
Blank, Rome, Comisky & McCauley
1200 Four Penn Center Plaza
Philadelphia, Pennsylvania 19103

Co-Counsel for Defendants:
Dash Industries, Inc.,
Jay Dash and Phillip Dash

David Stowell, Esquire
David Pash, Esquire
Kinsella, Boesch, Fujikawa & Towle
1875 Century Park East
Suite 1600
Los Angeles, California 90067

Counsel for Defendants:
Aerosonic Corporation, Inc.,
Herbert J. Frank and David S. Goldman

Joseph J. Brigati, Esquire
Jeffery B. Maletta, Esquire
Kirkpatrick & Lockhart
1800 M Street, N.W.
South Lobby
Washington, D.C. 20036

Co-Counsel for Defendants:
Aerosonic Corporation, Inc.,
Herbert J. Frank and David S. Goldman

Sheldon M. Jaffe, Esquire
Law Offices of Sheldon M. Jaffe, P.C.
1888 Century Park East
Suite 2100
Los Angeles, California 90067

Counsel for Defendant:
Edward P. Prescott

Joel S. Fass, Esquire
Colondy, Fass & Talenfeld
626 N.E. 124th Street
Miami, Florida 33161

Counsel for Defendant:
Elliot I. Eiseman

Jeffery Allan Tew, Esquire
Kirkpatrick & Lockhart
100 Chopin Plaza
Suite 2000
Miami Center
Miami, Florida 33131-2305

Counsel for Defendant:
Martin Blumenthal

Howard J. Privett, Esquire
Bill E. Schroeder, Esquire
McCutchen, Black, Veleger & Shea
600 Wilshire Boulevard
Los Angeles, California 90017

Counsel for Defendant:
Jose Luis Calonge
(aka Jose Luis Calonge Rivas)

Robert C. Gebhardt, Esquire
2151 LeJuene Road
Suite 310
Coral Gables, Florida 33134

Counsel for Defendant:
Jose Camprubi Sala

Roger Garrity
15292 Nantes Circle
Irvine, California 92714
Frankie Mae Garrity
15292 Nantes Circle
Irvine, California 92714

Mario Lamar
Attorney at Law
Lamar, Lamar & Associates, P.A.
3971 S.W. 8th Street
Miami, Florida 33134

Counsel for Defendants:
Tula Corporation and Talingo Corporation

Karla L. Bell, Attorney at Law
McKittrick, Jackson, Demarco & Peckenpaugh
4041 MacArthur Boulevard
5th Floor
Newport Beach, California 92660

Co-Counsel for Defendant:
Martin Blumenthal

Office of the U.S. Trustee
26 Federal Plaza
New York, New York 10278

Richard O'Connell, Esquire
Chapter 7 Trustee
Yost & O'Connell
161-24 Northern Boulevard
Flushing, New York 11358

Chapter 7 Trustee for Joseph A. Lugo, Jr.

Joseph A. Lugo, Jr.
415 E. 54th Street
New York, New York 10022

Charles Anshen, Esquire
16944 Ventura Boulevard
Encino, California 91316

Stuart D. Perlman, Esquire
30 North LaSalle Street
Suite 2630
Chicago, Illinois 60602

Delores Owens Cipparone
15 N.E. 123rd Terrace
North Miami, Florida 33161

Defendant, *In Pro Se*

Robert Mansell
c/o Huberman Margaretten & Straus
1380 Miami Gardens
North Miami Beach, Florida 33179

Rudolph A. Aragon, Esquire
Coffey, Aragon, Martin and Burlington, P.A.
2699 S. Bayshore Drive
Penthouse
Miami, Florida 33133

Co-Counsel for Defendant
Creditbank, Inc.

Jack Corinblit, Esquire
Corinblit, Shapero & Seltzer
3700 Wilshire Boulevard
Suite 820
Los Angeles, California 90010

Lester L. Levy, Esquire
Wolf Popper Ross Wolf & Jones
845 West Third Avenue
New York, New York 10022

C. Edward Simpson, Esquire
Michael J. Abbott, Esquire
Jones, Bell, Simpson & Abbott
800 Wilshire Boulevard
Fifth Floor
Los Angeles, California 90017

I declare under penalty of perjury that the foregoing is true and correct. Executed on August 1, 1989, at Los Angeles, California.

/s/ Ce Ce Medina
CE CE MEDINA

Nos. 89-55094 and 89-55128

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

vs.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

On Appeal From The United States District Court For The Central District Of California Honorable A. Wallace Tashima

PLAINTIFFS-APPELLANTS' SEPARATE OPENING BRIEF

JONES, BELL, SIMPSON & ABBOTT
C. EDWARD SIMPSON
MICHAEL J. ABBOTT
800 Wilshire Boulevard, Fifth Floor
Los Angeles, California 90017
Telephone: (213) 485-1555
Attorneys for Plaintiffs-Appellants Eugene W. Bell Trustee for the Liquidation of Joseph Sebag Incorporated and Laurence A. Schroeder Successor Trustee for the Liquidation of First State Securities Corporation

Bowne of Los Angeles, Inc., Law Printers (213)742-6600.

CERTIFICATION OF INTERESTED PARTIES
Case Nos.: 89-55094 and 89-55128
Certificate required by Circuit Rule 28-2.1

The undersigned counsel of record for plaintiffs and appellants Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation certify that the Securities Investors Protection Corporation, a named plaintiff in the district court action, and the following persons, all named defendants in the same action, have an interest in the outcome of this case.

Seymour Vigman
Aero Systems, Inc.
Aerosonic Corporation
Creditbank, Inc.
Dash Industries Inc.
Haberco, Inc.
Habers, Inc., Defined Benefit Pension Trust
Ibebafin, S.A.
Keops, S.A.
Magnetic Technologies Corporation
Talingo Corporation
Tula Corporation
Martin Blumenthal
Jose Luis Calogne, aka Jose Luis Calonge Rivas
Dolores Owens Cipparone, aka Dee Cipparone
Jay Dash
Phillip Dash
Isadore Diamond
Elliot I. Eiseman
Herbert J. Frank
Frankie Mae Garrity
Rodger W. Garrity
David S. Goldman
Jack A. Haber
Robert G. Holmes, Jr.
Joseph A. Lugo, Jr.
Robert J. Mansell
Gordon H. McNeil
Edward P. Prescott
Jose Camprubi Sala
Velma Shaw, aka Velma Shaw Meyers
Nettie Vigman
Lawrence West, aka Larry West

C. EDWARD SIMPSON
MICHAEL J. ABBOTT
JONES, BELL, SIMPSON & ABBOTT

By: _____

MICHAEL J. ABBOTT
Attorneys for Plaintiffs-Appellants Eugene W. Bell Trustee for the Liquidation of Joseph Sebag Incorporated and Laurence A. Schroeder Successor Trustee for the Liquidation of First State Securities Corporation

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IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

vs.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

PLAINTIFFS-APPELLANTS' SEPARATE OPENING BRIEF

I.

PRELIMINARY STATEMENT

This is the Separate Brief of Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated, and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation (the "Trustees")[1]

[1] The appeals before this Court have been consolidated. The Trustees and SIPC were directed to file a joint brief. The Trustees were given leave to file a separate brief addressing the

(Continued on following page)

addressing issues unique to their appeal from the summary judgment entered by the District Court in favor of Defendant Robert G. Holmes, Jr. ("Holmes") on the issue of causation under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder.[2]

II.

STATEMENT OF ISSUES

1. Did the District Court misapply the law of causation for injury arising out of a scheme or conspiracy to violate the antifraud provisions of the federal securities laws?

2. Did the District Court err in granting Holmes' Motion for Summary Judgment for lack of "loss causation" where genuine issues of material fact were presented concerning (1) Holmes' participation in a large scale scheme to manipulate six target securities; (2) Holmes' conspiring with those persons he asserts caused the Trustees' injury; and (3) Holmes' aiding and abetting the manipulation of those target securities that he asserts caused the brokerage firms' collapse?

(Continued from previous page)

Trustees' injury occasioned by violations of the antifraud provision of the federal securities laws. The Trustees join in the Statement of Jurisdiction and Standard of Review set forth in the Joint Brief.

[2] Section 10(b), 15 U.S.C. § 78j(b) (West 1981) and Rule 10b-5, 17 C.F.R. § 240. 10b-5.

III.

STATEMENT OF THE CASE

A. Nature of the Case

In late July 1981 two securities brokerage firms, Joseph Sebag Incorporated ("Sebag") located in Los Angeles and First State Securities Corporation ("FSSC") in Miami, were placed into liquidation under the Securities Investor Protection Act, 15 U.S.C. § 78aaa *et seq.* ("SIPA"). Both brokerage firms were victimized by a large scale scheme involving the manipulation of six securities traded in the over the counter market.[3] Both brokerage firms were used as conduits through which millions of dollars of illegal stock transactions were conducted.

It became clear that the same methods were used by the same perpetrators at both brokerage firms with the deliberate intent to operate a complex and sophisticated stock manipulation scheme. The scheme and the artificially inflated stock prices that resulted led to the financial instability and eventual collapse of both Sebag and FSSC when the scheme finally failed in July 1981.

This stock manipulation scheme drove the two brokerage firms into liquidation under SIPA and caused damages to the estates of Sebag and FSSC for which the Trustees seek redress.

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[3] Holmes and his co-defendants manipulated the securities of Aero Systems, Inc., Aerosonics Corporation, Bunnington Corporation, Creditbank, Inc., Dash Industries, Inc., and Osrow Products Corporation (hereinafter the "Target Securities").

B. Holmes, His Participation in the Manipulative Scheme to Defraud, And His Association with Other Defendants.

Holmes was one of the key individuals who participated directly in the defendants' manipulation scheme. Holmes had several accounts at FSSC through which he participated in the scheme. Holmes was the controlling shareholder and CEO of Aero Systems, one of the companies whose stock was manipulated. Holmes had a long history of suspect business transactions with the other participants in the scheme.

In May 1981, Holmes had known Joseph A. Lugo, Jr. ("Lugo")[4] for over fifteen years.[5] They had been through good and bad times together as they participated in several stock sales, mergers and transfers of a family of related companies that had their genesis in Aero Systems.[6] Some of these financial manipulations led to criminal and civil penalties for Lugo, Seymour Vigman ("Vigman")[7] and other participants in the scheme.

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[4] Lugo is a defendant and was the chief financial officer of FSSC. Lugo was the man inside who controlled most of the market in the Target Securities and who assisted in manipulating the market at FSSC by creating fake activity, setting artificially high prices, and restricting the floating supply of the Target Securities. C.R. 1310 at 6-19. Lugo's default has been entered in this action. He was later convicted of a felony in matters relating to tax law violations, and was sentenced to prison. (*United States of America v. Lugo*, No. S 87-00946-01 LBS (S.D.N.Y. filed July 11, 1988.)

[5] C.R. 1317 at 9, 15-17.

[6] C.R. 1317 at 18-21.

[7] Vigman was another long-time business associate of both Holmes and Lugo. Vigman was the subject of several civil and

(Continued on following page)

In the months leading up to May 1981, Holmes acquired a large number of Bunnington shares in the public market. Holmes bought most of his Bunnington stock through his accounts at FSSC,[8] which were handled by Lugo, Holmes' friend and broker.[9] Holmes purchased large blocks of Bunnington stock from Lugo at FSSC which Holmes resold in sixty-six carefully timed transactions through other broker-dealers.[10] These transactions and Holmes' participation in the manipulation scheme are discussed in the Joint Brief at 29-37.

Through private placements directly with Bunnington, Holmes acquired large blocks of approximately 90,000 shares of Bunnington stock which were restricted. 40,000 of these shares were to be freed from restrictions and could be sold into the public market in September 1981.[11] Holmes purchased these shares between 1979 and 1981 at prices averaging under three dollars per share. By May 1981, as a result of the scheme and conspiracy, Bunnington stock was manipulated by the scheme up to prices between $11 and $12 per share.[12]

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criminal proceedings as a result of numerous stock manipulation schemes he engineered. Vigman is also a convicted felon. C.R. 1317 at 11, 16-17, 20, 29-37.

[8] C.R. 1296, Ex. 3863.

[9] C.R. 1317 at 15; C.R. 1310 at 38.

[10] C.R. 1310 at 37-40.

[11] In May, 1981 Holmes had a Bunnington debenture which could be converted into 40,000 shares of Bunnington stock. Holmes converted the debenture into the 40,000 shares of Bunnington stock in July, 1981. C.R. 1317 at 92.

[12] C.R. 1317 at 95-98; C.R. 1309 at 15-18.

In May 1981 Holmes knew that if the price of Bunnington stock could be maintained at the $11-12 price range for only three more months,[13] Holmes' investment in Bunnington would be worth almost five times what he paid for it. It was with this background that Lugo and Holmes entered into the stock parking[14] transactions on May 20 and 29, 1981.

As an integral part of the manipulative scheme and to maintain the artificially inflated price of the Target Securities, Holmes, Lugo and the other defendants had to control the public supply of the Target Securities. One of the techniques used by Lugo and his cohorts was to employ FSSC and Sebag as repositories for the excess public supply of the manipulated stocks. As a consequence, as of May 18, 1981, FSSC's inventory reached an all-time high of $688,378, more than one-third of which was Bunnington stock.[15]

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[13] C.R. 1310 at 37-38.

[14] *SEC v. First City Financial Corp.* 688 F. Supp. 705, 719-24 (D.D.C. 1988). (" . . . a parking arrangement – a concealment of stock ownership achieved by placing the stock in an account in the name of a third party." *Id.* at 720.). *Cf. Rubin v. Posner*, 701 F. Supp. 1041, 1049 (D. Del. 1988). "Stock Parking" transactions have become the source of an ever-widening series of regulatory and criminal proceedings initiated by the Securities and Exchange Commission ("SEC") and the Justice Department. *See In the Matter of the Application of Whiteside & Company Inc.*, Exchange Act Release No. 26187, 1988 SEC Lexis 2063, 1 (Oct. 14, 1988) aff'd No. 88-4921 (5th Cir., July 24, 1989). The recent convictions in the *Boesky, Bilzerian, Drexel,* and *Jeffries* cases have all involved stock parking transactions. *Business and the Law; Is 'Stock Parking' like Jay Walking?*, N.Y. Times, March 14, 1988, at 2, col. 1.

[15] C.R. 1317 at 100.

At this point, FSSC was in jeopardy of violating the "net capital requirements" promulgated by the SEC,[16] pursuant to the federal securities laws. FSSC was required to file monthly reports of its net capital position to the National Association of Securities Dealers, Inc. ("NASD").[17] FSSC's net capital report for May 1981 would include all trades through May 21, 1981. FSSC's excess inventory, and the consequent reduction of net capital caused by the increase in inventory,[18] would have threatened FSSC's ability to remain in business and continue the manipulating scheme.

Through a carefully timed and orchestrated series of maneuvers, Holmes and Lugo were able to conceal a substantial block of Bunnington stock from NASD regulators, making FSSC appear to comply with the SEC net capital requirements.[19]

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[16] *See* SEC rule 15c3-1, 17 C.F.R. 240.15c3-1.

[17] This monthly report is called a "Focus Report" which details the financial condition of the brokerage firm as of the date of filing. FSSC reported its net capital to the NASD on a monthly basis, using the last Friday settlement as the closing date for financial statement and net capital computation. Trades as of May 21st were to be settled on May 29th, allowing five business days and one extra day to allow for the Memorial Day holiday, pursuant to the NASD Uniform Practice Code Paragraph 3504, Section 4. C.R. 1317 at 100 n. 118.

[18] By placing FSSC inventory stocks in customer accounts, FSSC reduced its net capital requirements as imposed by SEC regulations. Inventory stocks, unlike customer account stocks, are discounted in value in order to assess net capital compliance. This discount is commonly referred to as a "haircut". C.R. 1310 at 20 n.7

[19] C.R. 1317 at 100-102.

On May 20, 1981, Lugo entered a purchase order for 5,000 shares of Bunnington stock from FSSC's inventory account to Holmes' account at FSSC at a price of $61,250.00.[20] Holmes should have paid for this sale by May 28, 1981.[21] He did not.[22]

On May 29, 1981 Holmes sold the 5,000 Bunnington shares back to FSSC. This transaction would normally settle on June 5, 1981. However, Lugo was able to arrange an accelerated settlement of this sale for June 1, 1981.[23] Lugo also arranged for a check to be hand delivered to Holmes four days earlier than normal. This prepayment permitted Holmes to cover the original purchase with funds derived from FSSC.[24] Accomplishing this feat required precise timing and coordination among Lugo and Holmes.

To make the payment on June 1, 1981, FSSC had to borrow funds from the Stock Clearing Corporation of Philadelphia ("SCCP"). An employee of FSSC, Robert Reber ("Reber"), delivered the check which Holmes immediately endorsed, and which Reber then delivered to Holmes' bank for deposit.[25] On the same day, Holmes' band wired $61,250.00 to SCCP to be credited to the FSSC

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[20] C.R. 1317 at 15, 100-101.
[21] C.R. 1310 at 25.
[22] C.R. 1310 at 26.
[23] C.R. 1310 at 26.
[24] C.R. 1317 at 101.
[25] C.R. 1317 at 102.

loan account for payment of the stock originally purchased on May 20, 1981.[26] Ordinarily, payment would be made by a draft sent to FSSC's own bank to be credited to its bank account.[27] Through this parking transaction, Holmes "paid" for the 5,000 Bunnington shares with FSSC's own funds.[28] This transaction is expressly forbidden by SEC Rule 15c3-1, and had the net effect of increasing FSSC's inventory of Bunnington stock by 5,000 shares at a value of $61,875.00.[29]

The May 20 and 29, 1981 transactions facilitated the continuation of the manipulative scheme through June and into July 1981.[30] As a direct result of these transactions and the continued manipulation of the Target Securities, FSSC's net capital position substantially worsened.[31] If FSSC has simply ceased operations in May 1981, its losses would have been limited to $779,594. Because FSSC continued in business to July 24, 1981, its losses increased to $2,634,976.[32] To stabilize the price of the Target Securities and perpetuate the manipulative scheme, Sebag was forced to purchase $7 million worth of manipulated stock from FSSC for Sebag's inventory

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[26] C.R. 1317 at 103.
[27] C.R. 1317 at 101.
[28] C.R. 1317 at 103.
[29] C.R. 1310 at 28.
[30] C.R. 1310 at 24.
[31] C.R. 1310 at 34-36.
[32] C.R. 1310 at 35-36.

account.[33] If FSSC had stopped trading in May 1981, Sebag would not have collapsed.[34]

IV.
ARGUMENT

A. The District Court Failed to Apply The Appropriate Standard of Causation Where A Scheme To Defraud, or Conspiracy or Aiding and Abetting to Violate The Securities Laws Exists.

1. The District Court's Ruling.

The District Court did not issue an opinion and the parties are left to infer from the record the reasoning behind the Court's ruling.

The District Court, at oral argument, announced its tentative ruling that Holmes' conduct was too attenuated from the losses sustained to afford recovery by the Trustees.[35] Based upon the Court's order and comments from the bench, the Court analyzed the causation issue solely upon the isolated conduct of Holmes and not upon

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[33] C.R. 1317 at 108.

[34] C.R. 1317 at 109.

[35] At the hearing on the motions the Court stated:

> But on [Holmes'] remaining claims, I think my inclination is to grant the motion. I don't know if I can express myself any further. I think the causation claims, it's not so much whether or not there is an issue of fact. It's a question of, I think, attenuation and how far out can you spin the web and still find causation. I think that's almost what it amounts to. R.T. at 9.

the conduct of Holmes as a participant in a scheme to defraud.[36]

Holmes was only one of many persons engaged in the scheme to manipulate the Target Securities.[37] Consequently, Holmes' liability should have rested, not upon an analysis of his conduct in isolation from the conduct of his cohorts in the scheme, but upon established principles of causation previously set forth by this Court.

2. Injury From A Scheme to Defraud Arises from All of The Interacting Elements of The Scheme to Violate The Securities Laws.

The District Court clearly erred by using a legal standard that is inappropriate for determining causation where a scheme to defraud is alleged.

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[36] The court was misdirected in this regard by the very method employed by Holmes in seeking summary judgment. Holmes carved out his conduct, and urged the District Court to judge his conduct in isolation, from the conduct of his co-schemers and co-conspirators. Holmes filed *three* separate motions, each supported by separate exhibits, statements of uncontroverted fact and law and memoranda of points and authorities. C.R. 1273-1281 and 1290. One motion was directed to causation (C.R. 1281), one to claims asserted under RICO (C.R. 1277), and a third to SIPC's standing under Section 10(b) (C.R. 1275, 1290). To further complicate the record, Holmes submitted at least four separate proposed Summary Judgment Orders and Statements of Uncontroverted Facts and Conclusions of Law (C.R. 1341, 1342, 1343 and 1344). The District Court's modifications of those proposed Orders, Findings and Conclusions of Law clearly reveal that the motions were analyzed and decided on the basis of the purported conduct of Holmes individually rather than as a participant in the scheme to defraud. (C.R. 1342, 1343.)

[37] C.R. 1317 at 1.

The District Courts within the Ninth Circuit, citing *Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 381 (2d Cir. 1974), *cert. denied*, 421 U.S. 976 (1975), have held that where a *scheme to defraud has been alleged*, proximate cause is proven from all the interacting elements of the scheme, not by the isolated conduct of an individual participant. See *In re Washington Public Power Supply System*, 650 F. Supp. 1346, 1355 (W.D. Wash. 1986) and *Kafton v. Baptist Park Nursing Center, Inc.*, 617 F.Supp. 349, 350-351 (D. Ariz. 1985). In *Kafton*, the court held:

> In a rule 10b-5 scheme to defraud cause of action a plaintiff's injury stems not solely from a particular misstatement or omission but *from all the interacting elements of the scheme*. . . . In that instance, the causal nexus is not between a particular misrepresentation and the plaintiffs, but between the entire functioning scheme and the injury.

Kafton, 617 F. Supp. 350-51. (emphasis added)

The District Court erred by failing to apply this standard where there existed a connection between the "entire functioning scheme," in which Holmes participated, and the Trustees' "injury". *Id.* Consequently, the District Court's Findings of Fact and Conclusions of Law[38] are insufficient to support summary judgment in favor of Holmes. There is no clear finding that Holmes was not part of a conspiracy or scheme to violate Section 10(b) or Rule 10b-5.[39]

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[38] C.R. 1342 at 2-10

[39] Such a finding could not be made on the state of the evidence before the District Court as acknowledged by the

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3. Injury From A Conspiracy to Defraud Is Judged from The Entire Conspiracy, Not Just From Its Parts.

The District Court erred when it judged Holmes' conduct in isolation from the conduct of his co-conspirators, and concluded that Holmes was not a proximate cause of the Trustees' injury. However, in a conspiracy, causation must be judged by the entire conspiracy, not merely its constituent parts. *Beltz Travel Service, Inc. v. Int'l Air Transport Ass'n*, 620 F.2d 1360, 1366 (9th Cir. 1980), citing *United States v. Patten*, 226 U.S. 525, 544 (1913); *see also American Tobacco Co. v. United States*, 147 F.2d 93, 106 (6th Cir. 1944), *aff'd*, 328 U.S. 781 (1946).

In *Beltz*, this Court observed as follows:

> The Complaint alleged that the appellees were a part of an overall conspiracy in which they knowingly and willfully participated. We therefore apply the well-established principle that *"a conspiracy [is] not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole."*

620 F.2d at 1366 (emphasis added) (citations omitted).

Section 10(b) and Rule 10b-5 reach conspiracies to defraud. *Ferguson v. Omnimedia, Inc.*, 469 F.2d 194, 197 (1st Cir. 1972).[40] *See also Dasho v. Susquehanna Corp.*, 380 F.2d

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court in its Order Granting Summary Judgment (RICO claims). C.R. 1343 at 2-3.

[40] Significantly, the First Circuit in *Ferguson* instructed that summary judgment is ordinarily inappropriate where a

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262, 267 n.2 (7th Cir.), *cert. denied sub nom. Bard v. Dasho*, 389 U.S. 977 (1967); *Hoffman v. Halden*, 268 F.2d 280, 295-96 (9th Cir. 1959) (overruled on other grounds in *Cohen v. Morris*, 300 F.2d 24 (9th Cir. 1962)), *Herpich v. Wilder*, 430 F.2d 818, 819 (5th Cir. 1970), *cert. denied*, 401 U.S. 947 (1971).

In *Ferguson*, the court reversed the grant of summary judgment and held that a co-conspirator may be held accountable for another co-conspirator's acts, committed in the furtherance of their conspiracy:

> If [defendant] took part in the conspiracy, she may be held responsible for the acts of a coconspirator that actually misled the appellant into buying stock (such as her husband's furnishing of a false balance sheet), even if she herself did not participate in those acts.

Ferguson, 469 F.2d at 197.

Here, the Trustees presented substantial evidence of Holmes' overt acts committed in furtherance of the manipulative scheme to defraud. The evidence was sufficient for the District Court to find that there was a genuine issue of material fact as to whether Holmes conspired to violate RICO. The District Court erred in

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conspiracy has been alleged, since "[i]n a conspiracy case, agreement is rarely out in the open, and proof of conscious complicity may depend upon the careful marshalling of circumstantial evidence and the opportunity to cross-examine hostile witnesses. As in the present case, summary judgment procedures are often not a sufficient substitute for trial." *Ferguson*, 469 F.2d at 198, citing, *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 157 (1970).

considering the Trustees' claims against Holmes under Section 10(b) and Rule 10b-5 in a vacuum. It should have judged Holmes and his co-conspirators' actions together in determining the cause of the Trustees' harm. Accordingly, Holmes' summary judgment should be reversed, and this case should be remanded for trial.

4. The District Court Erred By Railing to Address Holmes' Liability for Aiding and Abetting The Manipulation of The Target Securities.

The District Court committed reversible error by granting Holmes' motion for summary judgment on the issue of causation when the Trustees submitted compelling evidence that was more than sufficient to create a genuine issue of material fact that Holmes aided and abetted the manipulation of Aero Systems and Bunnington stock.

The Ninth Circuit has repeatedly instructed that the elements of a claim for aiding and abetting under Section 10(b) and Rule 10b-5 consist of (1) the existence of an independent primary wrong, (2) actual knowledge by the alleged aider and abettor of the wrong and of his or her role in furthering it, and (3) substantial assistance in the wrong. *DCD Programs, Ltd. v. Leighton*, 833 F.2d 183, 188 (9th Cir. 1987); *Harmsen v. Smith*, 693 F.2d 932, 943 (9th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983); *SEC v. Rogers*, 790 F.2d 1450, 1460 (9th Cir. 1986).[41]

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[41] Secondary liability may attach even though the aider and abettor assisted in the scheme only by silence or inaction

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In the trial court, Holmes did not dispute that the Trustees presented substantial evidence of a primary wrong. In the first instance, Holmes conceded for purposes of his motion that Aero System stock was manipulated, and Holmes affirmatively argued that "the large concentration of artificially-inflated Bunnington and Aerosonic stock in FSSC's and Sebag's closing inventories was a substantial cause of the demise of the brokerage houses. . . . "[42]

The Trustees submitted overwhelming evidence of Holmes' knowing participation in the manipulation of Aero Systems stock[43] and Bunnington stock.[44] Holmes, using his concept of "sponsorship"[45], used public relations firms to disseminate false and misleading information[46], and used market makers to create investor interest in Aero Systems. Similarly, Holmes invested heavily in Bunnington stock, encouraged public relations firms and market makers to promote and market Bunnington stock,[47] and participated with Lugo in sham transactions to park unlawfully Bunnington stock in Holmes' account

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where a duty exists to disclose. *Strong v. France,* 474 F.2d 747, 752 (9th Cir. 1973). A duty to disclose arises from knowing of or assistance in a fraudulent scheme. *Id.*

[42] C.R. 1281 at 12-13.

[43] C.R. 1317 at 42-90.

[44] C.R. 1317 at 90-103.

[45] C.R. 1317 at 5-6.

[46] C.R. 1317 at 48-90; C.R. 1310 at 13-15.

[47] C.R. 1317 at 90-103.

at FSSC. These sham transactions created a false appearance of market activity, prevented a decline in the artificially inflated price of Bunnington stock,[48] and helped Lugo mask FSSC's net capital deficiency.

Holmes' transactions, including sales of Aero Systems stock to purchase Bunnington stock,[49] participation in the Bunnington stock manipulation,[50] and parking Bunnington stock in his account to aid Lugo in evading FSSC's net capital requirements,[51] constitute substantial assistance, sufficient to hold Holmes secondarily liable for all damages flowing from the manipulative scheme. *Rubin v. Posner,* 701 F.Supp. 1041, 1049 (D. Del. 1988) (secret agreement to park securities sufficient to constitute substantial assistance under Rule 10b-5 as well as loss causation). *See also SEC v. First City Financial Corp., Ltd.,* 688 F.Supp. 705 (D.D.C. 1988); *In Re Gas Reclamation, Inc. Securities Litigation,* 659 F.Supp. 493, 503 (S.D.N.Y. 1987).

5. The District Court Misapplied The Law of Causation And Its Ruling Is Contrary to Public Policy.

The District Court's ruling thwarts the remedial purposes of Section 10(b) and Rule 10b-5 by granting immunity to a participant in a series of fraudulent schemes that employed "novel" and "atypical" forms of fraud. The

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[48] C.R. 1309 at 15; C.R. 1310 at 23-29.

[49] C.R. 1310 at 44-45.

[50] C.R. 1317 at 90-99.

[51] C.R. 1310 at 25-29.

District Court's holding is contrary to the public policy behind the securities laws that "prohibit *all* fraudulent schemes . . . whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception." *A.T. Brod & Co. v. Perlow*, 375 F.2d 393, 397 (2d Cir. 1967) (emphasis in original).

The Trustees presented substantial uncontroverted evidence in the trial court that demonstrates Holmes' pivotal role in the scheme to defraud, his acts in furtherance of the manipulative conspiracy, and his aiding and abetting the manipulation of the Target Securities.

B. The Trustees Presented Substantial Evidence to Create Triable Issues of Material Fact that Holmes' Conduct in The Securities Law Violations Caused Their Injury.

Holmes argued in the District Court that even assuming that he had engaged in all of the securities law violations alleged by the Trustees, there was no genuine issue to be resolved concerning whether these violations caused losses to the brokerage firms.[52] Holmes asserted that neither the manipulation of the prices of the Target Securities nor the stock parking transactions caused any damages to FSSC or Sebag.

The Trustees submit that Holmes' participation in the manipulation of Aero Systems and Bunnington stock, the stock parking transactions that concealed FSSC's net capital violations – permitting FSSC to continue the manipulative scheme –, and his aiding and abetting securities

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[52] C.R. 1326 at 10.

law violations clearly demonstrate Holmes' activities in the manipulative scheme and conspiracy to defraud which proximately caused the Trustees' injuries. Because the Trustees presented substantial uncontroverted evidence of the causal link between the scheme to defraud, the conspiracy, assistance in violation of the federal securities laws and the Trustees' injuries, the trial court's decision should be reversed, and this case should be remanded for trial.

1. Holmes' Participation in The Parking Transactions Demonstrates His Responsibility for The Manipulative Scheme.

As set forth above, Holmes' participation in the parking transactions of May 20 and 29, 1981 establish that Holmes was an active participant in the broader fraudulent scheme involving Bunnington stock, among others. These transactions are analogous to the stock parking transactions presented in: *In the Matter of the Application of Whiteside & Company Inc.*, Exchange Act Release No. 26187, 1988 SEC Lexis 2063.1 (Oct. 14, 1988) *aff'd* No. 88-4921 (5th Cir., July 24, 1989).

In *Whiteside*, the SEC affirmed sanctions against the brokerage firm for engaging in stock parking transactions. The SEC condemned what it terms serious violations of the net capital reporting requirements, which were established for the protection of public investors. *Whiteside*, 1988 SEC Lexis 2063, at 11.

The participants in *Whiteside* used a scheme, similar to that used by Holmes and Lugo at FSSC, which

involved the transfer of positions from the firm's inventory account to the individual account of one of the firm's officers. The positions were parked off the books of the firm until the required report was filed. Then the positions were transferred back to the firm. The SEC had little difficulty dissecting these contrived transactions involving same day settlements, labeling them as "a sham," "false and misleading," and designed solely to "circumvent net capital requirements." *Id.* at 8.

The stock parking transactions engaged in by Holmes and Lugo bear all of the markings of the sham transactions condemned by the SEC in *Whiteside*. The questions and inferences concerning Holmes' participation in the overall manipulation, including the stock parking transactions, involved issues of material facts which should not have been decided by the District Court on a motion for summary judgment.

2. Holmes' Participation in The Bunnington and Aero Systems Manipulations Demonstrates His Responsibility for The Trustees' Injuries.

Holmes conceded for purposes of his Motion for Summary Judgment that Aero Systems stock was manipulated. Furthermore, Holmes affirmatively argued that "a large concentration of artificially-inflated Bunnington and Aerosonic stock in FSSC's and Sebag's closing inventories was a substantial cause of the demise of the brokerage houses. . . . "[53]

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[53] C.R. 1281 at 12-13.

The Trustees submitted substantial evidence that Holmes invested heavily in Bunnington stock, encouraged public relations firms and market makers to promote and market Bunnington stock, in addition to the transactions with Lugo to park Bunnington stock in Holmes' account at FSSC.

The net effect of these fraudulent activities was to create a false appearance of market activity in Aero Systems and Bunnington stock, maintain the artificially inflated prices of these and other stocks, and further the manipulative scheme.

Holmes' conduct was directly responsible for the damages to the estates of FSSC and Sebag and evidences Holmes' participation in the greater scheme to defraud.

3. The Existence of Genuine Issues Of Material Fact Should Have Precluded The Granting Of Holmes' Summary Judgment Motion

The manipulative scheme involved here is novel and complex. The net capital rule violations and the stock parking transactions which concealed these violations are key to understanding why Holmes' activities implicate him in this manipulative scheme and entitle the Trustees to recover damages against Holmes.

The Trustees should have been allowed to submit the evidence implicating Holmes in the stock manipulation scheme and conspiracy and stock parking transactions to a trier of fact. The Trustees should have been "given the full benefit of their proof without tightly compartmentalizing the various factual components and wiping the slate clean after scrutiny of each." *City of Long Beach v.*

Standard Oil Co. of California, 872 F.2d 1401, 1404-1405 (9th Cir. 1989), citing *Continental Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699 (1962).

V.
CONCLUSION

The Trustees submit that the District Court erred and the order granting summary judgment to Holmes should be reversed and this matter remanded for trial.

STATEMENT OF RELATED CASES

Plaintiffs and appellants Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation are aware of the following cases pending in the Ninth Circuit Court of Appeals which could be deemed related under Circuit rule 28-2.6:

Securities Investor Protection Corp., et al., vs. Vigman, et al., Nos. 84-6074, 84-6311, 764 F.2d 1309 (1985).

Securities Investor Protection Corp., et al., vs. Vigman, et al., No. 85-5786, 803 F.2d 1513 (1986).

PROOF OF SERVICE BY MAIL

STATE OF CALIFORNIA)
) ss.:
COUNTY OF LOS ANGELES)

I am a citizen of the United States and a resident of or employed in the City of Los Angeles, County of Los

Angeles; I am over the age of 18 years and not a party to the within action; my business address is 1706 Maple Avenue, Los Angeles, California 90015.

On August 1, 1989, I served the within Plaintiffs-Appellant's Separate Opening Brief in Securities Investor Protection Corporation, et al vs. Robert G. Holmes, Jr., on all parties interested in said action, by placing two true copies thereof enclosed in a sealed envelope, with postage thereon fully prepaid, in the United States Post Office mail box at Los Angeles, California, addressed as follows:

Jack I. Samet
Buchalter, Nemer, Fields & Younger
700 South Flower Street, Suite 700
Los Angeles, CA 90017-4183

Stephen C. Taylor
Sheppard, Mullin, Richter & Hampton
333 South Hope Street, 48th Floor
Los Angeles, CA 90071

I declare under penalty of perjury that the foregoing is true and correct.

Executed on August 1, 1989, at Los Angeles, California.

/s/ Ce Ce Medina
CE CE MEDINA

Nos. 89-55094 and 89-55128

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

Plaintiffs-Appellants,

VS.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

On Appeal From The United States District Court For The Central District Of California Honorable A. Wallace Tashima

PLAINTIFFS-APPELLANTS' REPLY BRIEF

STEPHEN C. TAYLOR
JOEL E. BONNER
MARK D. LARSEN
SHEPPARD, MULLIN, RICHTER & HAMPTON
333 South Hope Street, 48th Floor
Los Angeles, CA 90071
Telephone: (213) 620-1780

C. EDWARD SIMPSON
MICHAEL J. ABBOTT
JONES, BELL, SIMPSON & ABBOTT
800 Wilshire Boulevard, Fifth Floor
Los Angeles, CA 90017
(213) 485-1555

G. Robert Blakey
Notre Dame Law School
Notre Dame, Indiana 46556
Telephone: (219) 239-5717

CORNWELL & BLAKEY
1225 Seventeenth Street
Suite 2650
Denver, Colorado 80202
Telephone: (303) 295-2500

Attorneys for Plaintiff-Appellant Securities Investor Protection Corporation Incorporated and Laurence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation

Attorneys for Plaintiffs-Appellants Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag

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SECURITIES INVESTOR PROTECTION CORPORATION, EUGENE W. BELL, TRUSTEE FOR THE LIQUIDATION OF JOSEPH SEBAG INCORPORATED, AND LAURENCE A. SCHROEDER, SUCCESSOR TRUSTEE FOR THE LIQUIDATION OF FIRST STATE SECURITIES CORPORATION,

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VS.

ROBERT G. HOLMES, JR.,

Defendant-Appellee.

On Appeal From The United States District Court For The Central District Of California Honorable A. Wallace Tashima

PLAINTIFFS-APPELLANTS' REPLY BRIEF

Plaintiffs-Appellants Securities Investor Protection Corporation ("SIPC") and Eugene W. Bell, Trustee for the Liquidation of Joseph Sebag Incorporated, and Lawrence A. Schroeder, Successor Trustee for the Liquidation of First State Securities Corporation (the "Trustees") (collectively "Plaintiffs") submit the following Reply Brief on

appeal from the summary judgment entered in favor of Defendant-Appellee Robert G. Holmes, Jr. ("Holmes").[1]

I.

INTRODUCTION

Rather than directly address the issues squarely presented in Plaintiff's Opening Briefs. Holmes wholly disregards the controlling legal principle that a conspirator is liable for the acts of his co-conspirators. By admitting that Lugo and others caused the injuries to SIPC and the Trustees, Holmes effectively concedes that he also is liable for the injuries. Of equal significance, Holmes makes only passing reference to the central legal issue presented on appeal, *viz.*, whether there is a "purchaser-seller" standing requirement under the Racketeer Influenced and Corrupt Organizations Act ("RICO").

In seventy-five pages of factual minutiae, Holmes has dismembered the conspiracy, severed all illicit ties with his co-conspirators, twisted and distorted Plaintiffs' contentions and proffered implausible inferences of independent, rational and lawful conduct by Holmes. In the wealth of minutiae, the danger is run that the crucial questions in this appeal, legal and factual, may be forgotten.

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[1] As the non-moving parties, Plaintiffs are entitled to all permissible inferences and any doubts must be resolved in their favor. Plaintiffs-Appellants' Opening Brief ("Joint Brief") at pp. 7-9 and Plaintiffs-Appellants' Separate Opening Brief ("Trustees' Brief") (collectively "Opening Briefs").

The most telling omission in Holmes' brief, however, is his failure to deal with the hornbook law applicable to "conspiracy" and "scheme to defraud". The Amicus Curiae Brief of the Securities and Exchange Commission ("SEC") establishes beyond serious question that the principles applicable to "scheme to defraud" (at least where multiple parties are involved) are identical to those applicable to "conspiracy."[2] Vicarious liability attaches to those, like Holmes, who conspire to break the law and undertake an over act in furtherance thereof, provided the conspiracy causes harm to the plaintiff.

Holmes would have this Court believe that despite the District Court's finding that he participated in a RICO conspiracy, and despite the ample evidentiary record supporting that finding, Holmes did not participate in a conspiracy to manipulate securities other than Aero Systems. To prevail on the causation issue raised on appeal, however, Plaintiffs need only show that they have raised a single genuine issue of material fact as to whether Holmes participated in a conspiracy that caused injury to Plaintiffs. The evidence of Holmes' participation in such a conspiracy is, quite literally, massive.

Without a single reference to RICO, or any Supreme Court precedent construing the statute, Holmes argues that the "purchaser-seller" limitation on Rule 10b-5 should be imposed on the express right of action for a

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[2] Holmes passes off the Amicus Curiae Brief of the SEC as "irrelevant." (Opposition Brief, p. 50.) The SEC, however, is "the agency primarily responsible for the administration and enforcement of the federal securities laws. . . . " (Amicus Curiae Brief, p. 3.)

RICO violation predicated upon securities fraud. To the contrary, the text, structure, and legislative history – as well as the better judicial authority – demonstrate that RICO's remedial purpose cannot be so limited. Further, SIPC has standing to pursue RICO claims predicated on mail fraud and wire fraud, offenses which clearly are not subject to the "purchaser-seller" limitation.

Similarly, Holmes rejects Plaintiffs' position that proximate causation under the securities statutes and RICO are different, but offers no reasons to support his criticism. Plaintiffs' careful distinction between the language, policies and judicial construction of the two statutes stands virtually unchallenged on its merits.

Finally, Holmes' evidentiary objections, some of them made for the first time on this appeal, are without merit. The evidence and the record made before the District Court is admissible and more than sufficient to warrant a trial by jury.

The Order of Summary Judgment must therefore be reversed and this case remanded for trial.

II.

SIPC HAS STANDING UNDER RICO TO PURSUE THIS ACTION[3]

Holmes asserts that the judicially imposed purchaser-seller limitation applicable to the implied right of action

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[3] While SIPC's damages accrue as a result of a failure of Sebag and FSSC, those of the Trustees differ from those of

(Continued on following page)

under Rule 10b-5 applies with equal force to the express right of action under RICO. Holmes relies only on the Fourth Circuit's opinion in *International Data Bank v. Zepkin*[4] to support his argument, but never informs the Court that *Zepkin* did not include a claim based on the mail fraud statute.[5] The omission is significant, obviously, because SIPC presented evidence to the district court that Holmes committed acts of mail fraud and wire fraud.[6]

Holmes criticizes the Eleventh Circuit's opinion in *Warner v. Alexander Grant & Co.*,[7] as "without analysis or discussion,"[8] but offers none himself. Holmes completely fails to address Plaintiffs' extensive analyses of RICO offered to demonstrate the fundamental soundness of their position. Of critical important, Congress has not limited the express right of action granted by Section 1964(c) to those who have purchased or sold securities. Moreover, the predicate act of mail fraud contains no requirement that RICO plaintiffs buy or sell securities.

(Continued from previous page)

SIPC. In addition, standing to present these claims by the Trustees is not challenged by Holmes and is not an issue before the Court. The Trustees represent the estates of the debtors and have standing to recover, *inter alia*, damages the estates sustained as a result of trading in the manipulated securities prior to the liquidation of FSSC and Sebag. The District Court failed to recognize this distinction between SIPC and the Trustees.

[4] 812 F.2d 149 (4th Cir. 1987).

[5] *Zepkin* involved "only a Rule 10b-5 claim." Standing under other provisions of RICO was "not decid[ed]." *Id.* at 151.

[6] C.R. 1317, pp. 58-90.

[7] 828 F.2d 1528 (11th Cir. 1987).

[8] Opposition Brief, p. 68.

The Supreme Court has repeatedly held RICO's express text and legislative history, not its silence in the text or history, must guide RICO's interpretation.[9] The legislative history and the Supreme Court's mandate that RICO " 'be liberally construed to effectuate its remedial purposes' "[10] require that SIPC be allowed to bring this action, regardless of its status as a purchaser or seller of securities. Reversal of the order of summary judgment and a remand of this case is therefore appropriate.

III.

THE DISTRICT COURT ERRED BY GRANTING SUMMARY JUDGMENT BECAUSE THE EVIDENCE DEMONSTRATES THAT HOLMES ACTED IN FURTHERANCE OF A BROAD CONSPIRACY TO MANIPULATE TARGET SECURITIES AND VIOLATE THE SECURITIES LAWS AND RICO

Holmes attempts to limit his involvement in the conspiracy only to the Aero Systems manipulation[11], to sever all illicit ties with Lugo, Vigman and others, and to explain away his conduct as the product of rational, legitimate business dealings. His rationalizations and inferences simply do not ring true. As hard as he may try, Holmes cannot explain away the evidence presented to

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[9] *H.J. Inc. v. Northwestern Bell Telephone Co.*, 109 S.Ct. 2893 (1989); *United States v. Monsanto*, 109 S.Ct. 2657 (1989); *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 495 n.13 (1985).

[10] *Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479, 498 (1985), *quoting* Pub.L. 91-452, § 904(a), 84 Stat. 947.

[11] Holmes conceded for purposes of this motion that he participated in the manipulation of Aero Systems securities. C.R. 1281, p. 11. *See also* Joint Brief, p. 35, n.123.

the District Court by SIPC and the Trustees linking Holmes to the conspiracy and scheme to manipulate target securities.

A. The Evidence Demonstrates That A Common Goal, Manipulation Of The Target Securities Aero Systems And Bunnington, Was Motivated By The Greed Of Co-Conspirators Holmes, Vigman And Lugo.

Holmes, Vigman and Lugo had a common interest and goal to manipulate the prices of the target securities Aero Systems and Bunnington. The motive for this goal was greed. This common interest, and the acts they took in relation to each of these stocks, compels the inference of a carefully calculated conspiracy to manipulate the prices of both securities.

Holmes' interest in artificially inflating Aero Systems' prices flowed from his position with the company as president and its principal shareholder, holding 1,317,320 shares with a market value of over $7 million[12] in the spring of 1981. Indeed, he profited handsomely from the manipulation: between 1978 and 1981 Holmes sold 154,000 shares of Aero Systems, generating proceeds of $704,000.[13] Vigman, of course, also held large blocks of Aero Systems stock which he had obtained through Holmes' largess – the earlier exchange of worthless DCS stock for (eventually) tradable Aero Systems stock[14]

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[12] C.R. 1297, Exh. 5268; C.R. 1310, Exh. "E".

[13] C.R. 1310, p. 44, ¶ 111.

[14] C.R. 1317, pp. 33-36; Exhs. 5315 and 5316.

which Vigman partially sold for over $1.1 million in April and May, 1981.[15] Finally, Lugo made substantial trading profits through the manipulations and, indeed, reaped $863,000 in compensation from trading in the manipulated stocks from 1979 through the first four months of 1981.[16]

Identical interests motivated the three conspirators regarding Bunnington. Holmes had a substantial financial interest in keeping Bunnington's stock prices artificially high. In September of 1979, Holmes purchased a $100,000 convertible debenture which he converted into 40,000 shares of Bunnington in July 1981.[17] The restriction in sale of these shares was to be lifted in September 1981, only two months after the demise of FSSC and Sebag. Further, Holmes had also paid $150,000 to acquire an additional 50,000 shares of Bunnington (at $3 per share).[18] The "market" price of Bunnington in May 1981 was between $11 and $12 per share.[19] Thus, Holmes' 90,000 shares of Bunnington had a "market" value in excess of $1 million. Vigman was the largest shareholder of Bunnington, having a personal fortune tied up in 397,650 shares of Bunnington valued in excess of $4 million at the artificially inflated prices in effect shortly before the collapse.[20] Lugo also had a compelling interest in the common goal; there

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[15] C.R. 1310, p. 18, ¶ 26.

[16] C.R. 1310, p. 23, ¶ 41.

[17] C.R. 1317, p. 92.

[18] C.R. 1310, p. 45, ¶ 113.

[19] C.R. 1310, p. 54, ¶ 136.

[20] C.R. 1310, p. 54, ¶ 136; C.R. 1317, Exh. 6625.

was considerable sell pressure on Bunnington at the critical time.[21] and he had to maintain the artificially high price or FSSC would realize substantial losses in its trading account (which eventually occurred).[22]

Thus, each of the conspirators had compelling financial motives to manipulate the prices of both Aero Systems and Bunnington stocks[23].

When Lugo needed help to maintain the artificial price of Bunnington, he turned to Holmes and Vigman; when Lugo needed financing to buy Bunnington (and Aerosonic) in April, he turned to Vigman; when Lugo needed a trusted customer to assist in maintaining an artificial price for Bunnington, he turned to Holmes for market activity and parking; when Vigman and Lugo needed to maintain Bunnington's artificial price, they turned to Holmes to create market demand for Bunnington, tout Universal Silicon, and to pledge Aero

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[21] C.R. 1310, p. 19, ¶ 31.

[22] C.R. 1310, p. 36, ¶ 88.

[23] The fact of the conspiracy does not rest on financial motives alone. The conspiracy must be viewed in the historical relationship among the conspirators. Holmes owed much to Vigman; Vigman was described in 1980, as Holmes' "financial consultant, best friend and director" (C.R. 1317, pp. 1848-50), "confident" (*Id.*, p. 1852), and an "advisor" (*Id.*, p. 1761). Vigman claims that he was never paid for his advice to Holmes (*Id.* p. 2048). Holmes' substantial assistance in efforts to keep the price of Bunnington stock artificially high (see Section III.C. below and Joint Brief, pp. 29-34) were Holmes' "pay off" to Vigman and Vigman's brother-in-law, Diamond, who was a major shareholder and Chairman of Bunnington. Joint Brief, p. 30 n. 96.

Systems' stock to secure a $600,000 loan to buy Bunnington.[24] Thus, the three co-conspirators accomplished their common objectives together.

B. The Bunnington "Park" Is Direct Evidence Of Holmes' Complicity In The Broader Conspiracy To Manipulate The Target Securities.

In a revisionist attempt to legitimize his Bunnington parking transaction, Holmes argues for the first time on appeal that his May 29, 1981 sale of 5000 shares of Bunnington relates to his May 5, 1981 purchase of Bunnington shares, rather than his May 20, 1981 purchase.[25] Holmes' improvised argument that the applicable stock certificate numbers prove that he delivered the May 5, 1981 shares on June 1, 1981 to FSSC to cover the May 29, 1981 sale is illusory and meaningless.[26]

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[24] See Sections III.B.-F. below and Joint Brief, pp. 29-37.

[25] Opposition Brief, pp. 35-36.

[26] In his Opposition Brief, Holmes improperly purports to augment the record by identifying new evidence, to wit, the actual certificate numbers. (*Id.*, p. 36.) Holmes' attempt to introduce new evidence or argue new factual matters on appeal is barred by operation of law. *See Nissho-Iwai Am. Corp. v. Kline*, 845 F.2d 1300, 1307 (5th Cir. 1988); *Harkins Amusement Ent. v. Gen'l Cinema Corp.*, 850 F.2d 477, 482 (9th Cir. 1988), *cert. denied sub nom, United Artists Theater Circuit, Inc. v. Harkins Amusement Ent.*, 109 S.Ct. 817 (1989). Curiously, Holmes does not present any support for the new "evidence" to the Court. The certificate numbers are not, as Holmes suggests, available in the FSSC books and records. In any event, the certificate numbers are irrelevant.

It is wholly immaterial which certificate numbers were delivered by Holmes for his May 29, 1981 sale.[27] Lugo and Holmes "parked" Bunnington stock by arranging to prepay Holmes' May 29, 1981 sale and provide Holmes with the funds to cover his May 20, 1981 purchase in violation of Federal Reserve Board regulations.[28]

Holmes claims, nevertheless, that his May, 1981 trading in Bunnington shares was "in conformity with" legitimate trading activity.[29] The evidence establishes just the opposite. First, Holmes received an improper prepayment from his May 29, 1981 sale in order to pay for the May 20, 1981 purchase of Bunnington stock.[30] Second, an employee of FSSC hand-delivered the check representing the sale proceeds to Holmes for endorsement and deposit the same day.[31] Third, the sale was entirely inconsistent

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[27] C.R. 1310, p. 27, ¶ 58.

[28] Regulation "T" of the Federal Reserve Board requires payment by the customer before proceeds of the sale are released to the customer. 12 C.F.R. § 220.8 (1989).

[29] Opposition Brief. p. 40.

[30] The May 29, 1981 Holmes sale of 5,000 Bunnington shares "settled" on June 5, 1981, yet Holmes received a check for $61,875 from FSSC on June 1, 1981, four days earlier. Holmes' May 20, 1981 purchase of 5,000 Bunnington shares "settled" on May 28, 1981. Holmes claims he did not pay for these shares, however, until June 2, 1981. This was three business days after settlement of his May 20, 1981 purchase and one day after FSSC prepaid him for the sale. C.R. 1310, pp. 25-29. ¶¶ 48-63. This is not "in conformity with" ordinary customer transactions.

[31] C.R. 1310, p. 29, ¶ 63.

with Holmes' trading pattern in Bunnington stock.[32] Fourth, FSSC borrowed $125,000 to ensure the check to Holmes did not bounce.[33] Fifth, Holmes had significant motives to assist Lugo in concealing FSSC's deficiency – to protect the value of his own Bunnington holdings and perpetuate the broader conspiracy to manipulate target securities. Finally, the only expert to testify on the issue, Plaintiffs' expert James C. Foley, concluded that the transaction constituted parking of securities.[34]

In sum, it is Holmes, not SIPC and the Trustees, who ignores all meaningful evidence of the involvement and coordination needed between Lugo and Holmes to carry out the Bunnington park. The Bunnington park did not happen by chance, nor by Lugo's unilateral conduct. It was prearranged and planned. In substance, Holmes paid for the Bunnington shares involved in the parking transaction with FSSC funds.

As a result, Plaintiffs have no doubt, and there is at least a genuine issue of fact, that Holmes was a knowing participant in the greater conspiracy to defraud. Plaintiffs have come forward with "specific facts showing that

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[32] Holmes sold 53,900 shares of Bunnington stock on 64 different trades through various brokers between March 2, 1979 and June 16, 1981. His only "sale" at FSSC during this period was the 5,000 shares sold on May 29, 1981, the sale returning the parked shares to Lugo. C.R. 1310, p. 29, ¶ 63. (Holmes claims that Plaintiffs have misled the Court by failing to state that Holmes' 66 trades in Bunnington spanned a four year time frame (Opposition Brief, p. 32), yet 64 of the 66 trades occurred in just over two years.)

[33] C.R. 1310, p. 26, ¶ 54.

[34] C.R. 1310, pp. 27-28, ¶¶ 56-62.

there is a genuine issue for trial."[35] It was error for the District Court to grant summary judgment, because "the drawing of legitimate inferences from facts are jury questions, not those of a judge. . . . The evidence of [Plaintiffs] is to be believed and all justifiable inferences are to be drawn in [Plaintiffs'] favor."[36]

C. Holmes Conspired With Lugo In Creating Demand Volume For Bunnington In Furtherance Of The Bunnington Manipulation.

Based only on attorney conjecture, and without any support from expert testimony, Holmes contends that he could not have "constricted the floating supply" of Bunnington stock because he had more sales than purchases in 1981, and that these sales represented less than 1% of the total trading volume of 2.6 million shares in the over-the-counter market.[37] Holmes' unsupported analysis of the Bunnington manipulation misses the point.[38]

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[35] *Matsushita Elec. Indus. Co. v. Zenith Radio,*, 475 U.S. 574, 587 (1986).

[36] *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986).

[37] Opposition Brief, pp. 31-33. Holmes presented no expert testimony on causation issues other than the testimony of Plaintiffs' experts. As a result, there is no evidence that contradicts or rebuts the opinions of expert witnesses Foley and Torkelson. Holmes' citation to Plaintiffs' experts is out of context and of no moment.

[38] SIPC and the Trustees do not contend that Holmes and Lugo were solely responsible for the Bunnington manipulation. Other participants included, *inter alia*, defendants Garrity, Vigman, Diamond and McNeil.

On nine separate occasions between May 31, 1979 and May 20, 1981 Holmes' purchases of Bunnington represented 51% of NASDAQ average daily volume.[39] On these occasions Holmes conspired with Lugo in creating demand volume, thus stimulating interest in Bunnington to the investing public during periods of low trading.[40]

In the nine purchase transactions with FSSC, Holmes played a dominant role and assisted Lugo in controlling the market on the days that he traded.[41] Further, the evidence is clear that Holmes traded on inside information,[42] received preferential treatment from Lugo and

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[39] C.R. 1310, p. 40, ¶ 98.

[40] Lugo, as the primary market maker of Bunnington, relied on Holmes and other select customers to purchase the stock, on a given day or at a given time, in order to maintain artificially the market price. Holmes' effort to hide in the larger group of Bunnington purchasers is a ludicrous attempt to mask his participation in the manipulation of Bunnington's price. Opposition Brief, p. 34. Unlike normal investors, Holmes and his co-conspirators traded Bunnington with the intent and effect of manipulating the market price. C.R. 1310, pp. 40-41. ¶¶ 99, 102.

[41] C.R. 1310, p. 40, ¶ 99. Holmes assisted Lugo in soaking up the floating supply of Bunnington stock up purchasing Bunnington from FSSC. *Id.*

[42] Holmes claims that he did not trade on inside information when he bought Bunnington shares on May 5, 1981, one day prior to Bunnington's falsely optimistic announcement that it was acquiring Universal Silicon. Opposition Brief, pp. 48-49. As in numerous other instances, Holmes argues that the timing of his purchase was purely fortuitous, yet Holmes himself wired the false press release to Moore Schley on May 6, 1981. This argument by Holmes, as all others he makes about

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sold Bunnington only in small lots through other brokers at virtually no profit.[43] These are indicia of participation in a market manipulation. Further, following the collapse of FSSC and Sebag, Holmes renewed his effort to assist co-conspirator Vigman in maintaining artificially the price of Bunnington.[44] It is for the jury to decide whether Holmes' trading was rational, economically motivated, or as SIPC and the Trustees contend, part of the greater conspiracy and scheme to defraud.

D. Plaintiffs' Damages Are Not Limited By The Initial Net Capital Deficiency At FSSC.

Holmes argues, repeatedly, that it is inconsistent and illogical to blame him for injuries to SIPC and the Trustees when several of the events causing the injuries

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what the facts mean, merely serves to emphasize the need to submit them to a jury for resolution.

[43] C.R. 1310, pp. 38-39, ¶¶ 94, 96-97.

[44] Notwithstanding Holmes' claim that he believed Bunnington was a stock with "merit" (Opposition Brief, p. 47), the evidence clearly indicates that his purchases were made to fill the demand void left by the demise of market makers FSSC and Sebag, as an accommodation to his co-conspirator Vigman, the largest shareholder in Bunnington. Holmes' extensive post-collapse Bunnington stock purchases made over time with $600,000 borrowed against his Aero Systems' stock (C.R. 1317, p. 98) is compelling evidence of a pre-collapse conspiracy between Holmes and his long-time friend, advisor and financial consultant, Vigman, to artificially maintain the value of Bunnington stock.

occurred after April 1981, the time when FSSC first experienced a "net capital deficiency."[45] It is Holmes' claims, however, that are syllogistic nonsense.

There is no reason why losses sustained by a brokerage firm in liquidation are limited by the events preceding the initial determination of a "net capital deficiency."[46] This is particularly significant where, as here, the initial determination of a "net capital deficiency" is concealed from regulators to allow the conspiracy to continue and associated losses escalate dramatically during the period of concealment and continued manipulation of target securities. Hence, it is pure sophistry to suggest, as does Holmes, that April 1981 was the date of injury or that subsequent events could not possibly have caused losses to SIPC and the Trustees.

A net capital deficiency is not a loss, as Holmes contends, but only a warning of potential loss.[47] Proper

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[45] Opposition Brief, pp. 26-28, 41-42. Holmes apparently confuses the March 1981 "reserve deficiency" at FSSC with an April 1981 "net capital deficiency," underscoring Holmes' misunderstanding of what a "net capital deficiency" represents and how it relates to the losses sustained by SIPC and the Trustees.

[46] Holmes has not cited any authority nor advanced any reason why losses would be limited or determined by events preceding a "net capital deficiency."

[47] See 17 C.F.R. § 240 15c3 (1988). Equally true, there is no merit to Holmes' contention that his role in impairing FSSC's net capital should be evaluated strictly as an $18,000 event. (Opposition Brief, pp. 41-42.) In his Opposition Brief, Holmes disingenuously attempts to single out the Bunnington "park"

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reporting of such deficiencies has the effect of giving a warning signal to regulators who will cause the brokerage firm to limit actual losses. Failure to make a proper report has the opposite effect. That is, brokerage firms, such as FSSC, who continue to operate while in a condition of net capital deficiency will sustain greater losses upon ultimate liquidation.

In the case of FSSC, its net capital deficiencies in 1981 resulted primarily from a massive accumulation, or "undue concentration," of the target securities, Bunnington and Aerosonic, in FSSC's trading account, an accumulation that began by April 1981. Had FSSC reported its true trading account positions, the regulatory process would have required a liquidation, or forced sale, of target securities in the trading account to achieve compliance with the net capital rule.[48] Such a forced sale, however, was undesirable to the conspiracy, because it would have flooded the market with shares of these securities, thereby depressing artificially high prices of

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as the only act of concealment of FSSC's "net capital deficiency." (*Id.*) It is abundantly clear that while Holmes was not solely responsible for the concealment, he facilitated FSSC and Sebag's ability to remain in business and expand their trading positions to "undue concentration" levels greatly in excess of their capitalization. SIPC and the Trustees, as a result, suffered total losses in excess of $30 million. This facilitation shows Holmes' complicity in the exponential accumulation of losses.

[48] If net capital is impaired by risks associated with large accumulations of inventory, regulators traditionally require an infusion of new capital or immediate liquidations of inventory at the market to achieve compliance with the net capital rule. C.R. 1310, p. 21, ¶ 36.

the target securities.[49] Instead, in furtherance of the conspiracy, Lugo falsified the FSSC net capital reports to deceive regulators and prevent the artificial market prices from decreasing.[50]

Thus, the concealment by Lugo, with Holmes' knowing and active assistance, allowed the conspiracy to continue manipulating target securities. During this period, these manipulations increased damages to SIPC and the Trustees to massive proportions.

E. Holmes' Admitted Manipulation Of Aero Systems Was Part Of The Larger Conspiracy To Manipulate The Target Securities.

Holmes portrays his admitted participation in the manipulation of Aero Systems stock in March and April 1981 as a purely fortuitous, coincidental event that has no connection whatsoever to the manipulations of Bunnington and Aerosonic.[51]

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[49] C.R. 1273, p. 101.

[50] The April-July 1981 concealment enabled Lugo to continue buying target stocks Bunnington and Aerosonic for FSSC's trading account in furtherance of the conspiracy. Total losses from the FSSC liquidation were approximately $4 million. C.R. 1342, p. 3. Sebag, by reason of its June-July 1981 purchases of manipulated target securities from FSSC for its trading account, experienced a massive net capital deficiency and losses of approximately $26.2 million. C.R. 1273, p. 139, Exh. 10,043. Had the "net capital deficiency" at FSSC been reported properly in April 1981, the losses incurred by FSSC and Sebag would have been substantially less than actually realized. C.R. 1310, p. 35, ¶ 83.

[51] Opposition Brief, pp. 18-50.

To support his position, Holmes separates, dissects, and mischaracterizes Plaintiffs' contentions.[52] Holmes also mischaracterizes the evidence by presenting individual facts out of context and in an environment that overlooks the underlying conspiracy.[53] He also ignores the effect of his admission that he participated in the manipulation of Aero Systems.

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[52] For example, Holmes contends Plaintiffs contradict themselves by contending that "profits" to FSSC caused "damages" to FSSC (Opposition Brief, p. 27), and by contending that a "capital infusion" can impair the net capital of a brokerage firm. *Id.*, pp. 30-31. To make his point, Holmes mischaracterizes Plaintiffs' contentions. Plaintiffs contend that Holmes and his co-conspirators successfully manipulated the price of Aero systems in 1981, as conceded by Holmes, then used the proceeds from sales of Aero Systems to underwrite the manipulations of target stocks Bunnington and Aerosonic. Plaintiffs further contend that when FSSC and Sebag could no longer conceal "net capital deficiencies" arising from "undue concentrations" in Bunnington and Aerosonic in July, 1981, regulators were forced to liquidate the brokerage firms. In effect, the "profits" or "capital" from the Aero Systems manipulation were reinvested into the RICO enterprise.

[53] Holmes contends it was Lugo's use of the proceeds from Vigman's sales of Aero Systems, not the source of funds, that give rise to Plaintiffs' damages. Opposition Brief, p. 30-31. Such a "source of funds" argument would only have significance if there was no evidence of a conspiracy to reinvest illicit proceeds or manipulate other target securities. However, there is abundant evidence of such a conspiracy and manipulation scheme. Moreover, Lugo's use of the funds made available by the Aero Systems manipulation to invest in the Bunnington manipulation would provide a direct benefit to Holmes, who traded in Bunnington and held a sizeable Bunnington convertible debenture. C.R. 1310, pp. 17-19, 38, ¶¶ 24-31, 92.

Holmes' arguments, however, only emphasize that there are disputed issues of material fact, entitling the Plaintiffs to present their claims to a trier of fact. The evidence of Holmes' participation in the Aero Systems manipulation demonstrates Holmes' participation in the conspiracy with Lugo, Vigman and others.

First, the *modus operandi* of the Aero Systems manipulation is similar to that used in the Bunnington manipulation.

(a) False press releases were published by Aero Systems and Bunnington;[54]

(b) Holmes solicited Moore Schley to take an interest in Aero Systems and Bunnington in order to support the prices of the respective stocks;[55]

(c) Lugo dominated and controlled the market in both securities;[56] and

(d) The capital of FSSC was put at risk to underwrite the Aero Systems and Bunnington manipulations.[57]

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[54] C.R. 1317, pp. 58-88, 95-97. Holmes erroneously claims that there is no evidence that the Bunnington press release he sent to Moore Schley was false. Opposition Brief, p. 46. Like the Aero Systems press releases, the May 6, 1981 Bunnington press release falsely "hyped" Bunnington in connection with its announced acquisition of Universal Silicon. See C.R. 1309, p. 17, ¶ 21.

[55] C.R. 1317, pp. 72, 95.

[56] C.R. 1310, pp. 40, 50, ¶¶ 99, 124.

[57] C.R. 1317, pp. 105-108.

Second, the evidence shows that the Aero Systems manipulation was used to generate cash used by the conspiracy to finance the manipulation of Bunnington.[58]

Third, it was not purely fortuitous that Vigman, who was an officer and the largest shareholder of Bunnington, profited significantly from the Aero Systems manipulation while Holmes, the President and largest shareholder of Aero Systems, was in a position to profit significantly from the Bunnington manipulation.[59]

Fourth, it was Vigman who advised and counseled Holmes concerning the promotion and "hyping" of Aero

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[58] Holmes argues that funds made available by the Aero Systems manipulation could have been left untouched or used for proper purposes without any negative impact on FSSC or Sebag. Opposition Brief, p. 30. Holmes' argument ignores, once again, the underlying conspiracy to manipulate the target securities. In furtherance of the conspiracy, proceeds from the Aero Systems manipulation were used to invest in target securities Bunnington and Aerosonic.

[59] C.R. 1310, pp. 18, 38, ¶¶ 26, 92. Holmes contends that by lifting the selling restrictions on Vigman's April-May 1981 sales of Aero Systems, Holmes merely acted as required by Rule 144 of the Securities Act of 1933. Opposition Brief, p. 52. However, Holmes did much more to assist co-conspirator Vigman. The act itself is normally required. It is the expedited nature of it in the time of crisis that raises the inference that Holmes' acts were abnormal. Further, as Holmes knew, Vigman was timing his sales of Aero Systems to FSSC in April-May 1981 to take full advantage of false press releases reviewed and approved by Holmes and Vigman. C.R. 1317, p. 52, n. 61; C.R. 1310, Exh. "E". Vigman then deferred receipt of the proceeds so co-conspirator Lugo could use the proceeds to continue the manipulation of other target securities. C.R. 1310, pp. 18-19.

Systems stock through false and misleading press releases.[60]

Fifth, there was a close proximity between the successful Aero Systems manipulation (March and April 1981) and the continued Bunnington manipulation (April, May, June, and July 1981).[61]

F. Holmes Cannot Sever The Numerous Links Between His Conduct And That Of His Co-Conspirators.

The central theme running through Holmes' Opposition Brief is that there is insufficient evidence to link Holmes to the conduct of Lugo, Vigman and other co-conspirators who, Holmes concedes and indeed contends, are directly responsible for the injuries to SIPC and the Trustees.[62] None of his examples, however, are the least bit compelling. Rather, each example demonstrates that there are disputed facts and inferences which entitle SIPC and the Trustees to a jury trial.[63]

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[60] C.R. 1317, pp. 44, 49-54.

[61] *Id.*, pp. 58-62.

[62] Opposition Brief, pp. 29, 30, 33-34, 36-41, 44-49.

[63] Holmes contends, *inter alia*, that "the pledging of Aero stock by Sebag and FSSC is not even alleged to have been connected to any conduct by Holmes," that the brokers could have used collateral other than Aero Systems to secure loans to buy target stocks, that Lugo's decision to use the proceeds of sales of inflated Aero Systems stock to buy Bunnington and other target stocks is unconnected to Holmes, and that Holmes' decisions to buy, sell and promote Bunnington were unrelated to the alleged conspiracy. Opposition Brief, pp. 29, 30, 33-46.

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The evidence is more than sufficient to ask a jury to infer that Holmes participated in, and assisted Lugo, Garrity, Vigman and others in, a broad conspiracy and scheme to manipulate the target securities and numerous RICO violations.[64]

The only nexus that Holmes apparently concedes would be sufficient is direct evidence that Holmes knew and approved of the brokers' pledging, that he knew and approved of FSSC's purchases of Bunnington and that he traded and promoted Bunnington with full knowledge of its manipulative impact. This is not the standard. "[O]bvious evidence of such operations is seldom available in any case, for the nature of the fact to be proved, concealed participation, does not lend itself to demonstration by direct evidence."[65] "[I]f the evidence is such that a reasonable jury could return a verdict for the nonmoving party," "summary judgment will not lie."[66] SIPC and the Trustees have met that burden.

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Once again, Holmes has pulled individual pieces of the conspiracy out of context for microscopic inspection. Contrary to his contention, Lugo and Holmes did not act independently in "pursuing [their] own lawful economic objectives." *Id.*, p. 54. Rather, Lugo acted in concert with Holmes, Vigman and others in pursuit of a common purpose – the manipulation of the target securities. SIPC and the Trustees have presented ample evidence supporting a logical inference of such a conspiracy. *See* C.R. 1317; 1310; 1309.

[64] Joint Brief, pp. 1-6.

[65] *Johnson v. Chilcott*, 658 F. Supp. 1213, 1223 (D. Colo. 1987); *See also Miller v. Schweikhart*, 413 F. Supp. 1062, 1065 (S.D.N.Y. 1976).

[66] *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986).

IV.

THE ACTS OF HOLMES AND HIS CO-CONSPIRATORS WERE THE PROXIMATE CAUSE OF INJURY TO SIPC AND THE TRUSTEES

Holmes seeks to divorce his acts from those of the remaining defendants in an effort to escape liability both for his egregious conduct and that of his fellow co-conspirators. To do so, Holmes argues that SIPC and the Trustees must "establish a direct causal relationship between the alleged wrongdoing of the defendant and the injury . . . whether or not there was a broader scheme of which [Holmes'] conduct was a part."[67]

Holmes blithely ignores the time-honored rule that co-conspirators are "liable for the acts of all members of the conspiracy in furtherance of the conspiracy, regardless of the nature of [the conspirator's] own actions."[68] Holmes' position concerning the law of conspiracy is in error. If adopted, it would also be unique and inconsistent with the principles followed in common law and statutory conspiracy claims for relief.[69] Whether analyzed under Rule 10b-5 or RICO, the correct rule is that persons who agree among themselves to break the law and intentionally commit an act in furtherance of the conspiracy

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[67] Opposition Brief, p. 60.

[68] *Beltz Travel Serv. Inc. v. Int'l Air Transp. Ass'n*, 620 F.2d 1360, 1367 (9th Cir. 1980).

[69] *See e.g. Kashi v. Gratsos*, 790 F.2d 1050, 1054-55 (2d Cir. 1986); *Beltz*, 620 F.2d 1360, 1367; *Halbertstam v. Welch*, 705 F.2d 472, 487 (D.C. Cir. 1983); *Rice v. Janovich*, 109 Wash.2d 48, 49-52, 58-62, 64-67, 742 P.2d 1230, 1232, 1236-38, 1239-40 (1987).

are liable for all the damages caused by any other act undertaken in furtherance of the conspiracy.[70]

A. The Proximate Cause Determination In Scheme To Defraud And Conspiracy Cases Is Between The Entire Functioning Scheme And The Loss.

Proximate cause in scheme to defraud and conspiracy cases is not proved by viewing the isolated conduct of each participant and asking whether that conduct alone caused damage. To the contrary, "[i]n a Rule 10b-5 scheme to defraud [cause of action] a plaintiff's injury stems not solely from a particular misstatement or omission but from all interacting elements of the scheme."[71] Further, " 'a conspiracy [is] not to be judged by dismembering it and viewing its separate parts, but only by looking at it as a whole.' "[72] Therefore, because Plaintiffs have presented a genuine issue of material fact that Holmes conspired with his co-defendants, the correct causation test is to ask whether any act by one of Holmes'

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[70] *Beltz*, 620 F.2d at 1367; *Ferguson v. OmniMedia, Inc.*, 469 F.2d 194 (1st Cir. 1972). Holmes' contention that he never traded through Sebag and never had more than a passing acquaintance with Garrity is of no consequence. Opposition Brief, p. 26, n. 84. Holmes' acts in concert with Lugo suffice to establish his role in the conspiracy. Similarly, Garrity and Sebag assisted Lugo and FSSC in the conspiracy to manipulate the target securities. C.R. 1310, p. 31, ¶ 71.

[71] *Kafton v. Baptist Park Nursing Center, Inc.*, 617 F. Supp. 349, 350 (D. Ariz. 1985), *citing Schlick v. Penn-Dixie Cement Corp.*, 507 F.2d 374, 381 (2d Cir. 1974).

[72] *Beltz*, 620 F.2d at 1366 (citations omitted).

co-conspirators caused Plaintiffs' damages. It is not necessary for Plaintiffs to demonstrate that any overt act of Holmes is the proximate cause of Plaintiffs' injury.

For example, in *Halberstam v. Welch*,[73] the court found that a civil conspiracy existed to commit burglary and sell the stolen goods. The defendant performed services as a bookkeeper for the scheme, and had lived with the burglar for a number of years. During one of the burglaries, a killing took place. In the wrongful death action, plaintiff alleged that the killing during the commission of a burglary was within the scope of the conspiracy to steal goods in order to sell them later. The District of Columbia Circuit held:

> A conspirator can be liable even if he neither planned nor knew about the particular overt act that caused injury, so long as the purpose of the act was to advance the overall object of the conspiracy.[74]

As set forth above, the District Court expressly found a genuine issue of material fact that Holmes agreed to violate RICO. Plaintiffs have also presented evidence that Holmes undertook overt acts in furtherance of the conspiracy. The appropriate causation nexus in such a case must be between the entire scheme and all the acts of the conspirators and the harm "so long as the purpose of the act was to advance the overall object of the conspiracy."[75] This includes liability on Holmes' part for the acts of

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[73] 705 F.2d 472, 487 (D.C. Cir. 1983).

[74] *Halberstam*, 705 F.2d at 487; *see also Beltz*, 620 F.2d at 1367.

[75] *Id.*

Lugo, Vigman, Garrity, and other defendants undertaken in furtherance of the agreement to manipulate securities and violate RICO.

Bloor v. Carro, Spanbock, Londin, Rodman & Fass,[76] cited by Holmes, has no impact upon the principles of conspiracy and causation at issue in this case. The plaintiff-trustee in *Bloor* did not allege a conspiracy against the defendant law firm. The trustee in *Bloor* brought a lawsuit against a number of defendants, including Peat, Marwick & Main, accountants for the filed Investment Funding Corporation of New York, and Carro, Spanbock, the firm's lawyers. In addressing the claims made against the law firm, the Second Circuit noted "[t]he district court found that the Trustee's claims against the law firm suffered from the same causation defects as those against PMM."[77] A review of the allegations against Peat, Marwick clearly reveals that the trustee never alleged any conspiracy claim against the accountants.[78] The district court never addressed the law of causation in conspiracy cases as to the law firm because, if it had, the court would have applied principles of causation applicable to conspiracy cases, instead of the principles applicable to non-conspiracy cases such as that brought against Peat, Marwick. The district court did not address issues of conspiracy with respect to either the accountants or the law firm. In contrast, as set forth above and as expressly found by

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[76] 754 F.2d 57 (2d Cir. 1985)

[77] *Bloor*, 754 F.2d at 60. *See also In re Investors Funding Corp. of New York Secs. Lit.*, 566 F. Supp. 193, 201 (S.D.N.Y. 1983).

[78] *In re Investors Funding Corp. of New York Secs. Lit.*, 523 F. Supp. 533, 542 (S.D.N.Y. 1980).

the District Court below, Plaintiffs herein have already presented a genuine issue of material fact that Holmes violated RICO and agreed with others to do so. Holmes' attempt to carve out his culpable conduct as if no conspiracy exists must therefore be rejected.

Holmes attempts to assert that loss causation between his acts and the damages sustained is required in this conspiracy case; however, Holmes never addresses the causation requirements of the RICO claims against him. Further, Holmes conveniently ignores the rule that conspirators are liable for the acts of their co-conspirators undertaken to further the illegal agreement. The District Court found genuine issues of material fact that Holmes violated each subsection of RICO and conspired with his co-defendants to do so.[79] Holmes ignores these findings in an effort to sweep RICO's broad remedial frame work under the restrictive rug of "loss causation."

The standard is clear: persons who conspire to violate RICO are liable for all loss caused "by reason of" the act of any co-conspirator. Holmes cannot escape the simple standard that injury caused by reason of the violation is actionable under Section 1964(c). Further, Holmes has no authority for his implied assertion that plaintiffs in a civil conspiracy case must "establish a direct causal relationship"[80] between his conduct and the loss because the law is exactly the opposite. Therefore, the grant of summary judgment should be reversed and this case remanded for trial.

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[79] C.R. 1343, p. 2 ¶¶ 1-5.

[80] Opposition Brief, p. 60.

B. Holmes Was An Integral Player In The Conspirarcy [sic] And Scheme To Defraud, Unlike The Defendants In *Bloor* and *Miller*.

Holmes erroneously cites to *Bloor* and *Miller v. Schweickhart*[81] for the proposition that Plaintiffs must present a triable issue that Holmes' activities, in isolation, were the proximate cause of the massive damage sustained in this case.[82] In doing so, Holmes misreads *Bloor* and disingenuously misrepresents the nature and scope of the proof against him. Holmes also ignores the factual dissimilarities of *Miller* which, on its facts, has little to do with this case. Further, Holmes conveniently minimizes the RICO allegations against him in an attempt to rid himself of responsibility for the criminal conduct at issue in this case and the harm proximately caused by the culpable acts.

In *Bloor*, a bankruptcy trustee alleged that the law firm representing Investors Funding Corporation of New York had assisted in the preparation of SEC registration statements, 10-Ks, annual reports and proxy statements which failed to disclose or misrepresented material information. Funds invested by misled investors were later "allegedly funneled into unwise investments or diverted. . . . "[83] Bloor's only factual allegation concerning causation was that but for the infusion of funds as a result of the misleading documents, the principals of the defunct investment firm would not have had any funds

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[81] 413 F. Supp. 1062 (S.D.N.Y. 1976).

[82] Opposition Brief, pp. 54-61.

[83] *Bloor*, 754 F.2d at 62.

with which to " 'perpetrate and maintain the Fraud.' "[84] The Second Circuit agreed with the defendant's argument, holding that "the failure of the corporation to use proceeds wisely or the theft of corporate funds by officers was hardly a reasonably foreseeable result, let alone a direct result" of the law firm's activities.[85]

Bloor cannot be authority for the affirmance sought by Holmes because it did not address legal or factual issues comparable to those present in this case. First, *Bloor* did not involve persons who conspired to violate RICO. In fact, *Bloor* is not a conspiracy case.[86] Second, *Bloor* is readily distinguishable on its facts because of the *de minimus* involvement of the defendant law firm in the harm sustained by Investors Funding Corporation. In contrast, SIPC and the Trustees have presented evidence that Holmes committed overt acts in furtherance of the conspiracy and affirmatively acted to perpetrate the stock manipulations.

Moreover, the Second Circuit held in *Bloor* that the defendant law firm could not have foreseen the theft of corporate funds by others. In contrast, it was foreseeable to Holmes that the damage sustained by Plaintiffs would

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[84] *Id.*

[85] *Id.*

[86] Plaintiffs herein have presented evidence, and the district court expressly found, that Holmes invested illicitly gained income into an enterprise, obtained control over an enterprise through illegal acts, associated with an enterprise and conducted its affairs through a pattern of racketeering and conspired with his co-defendants to violate RICO. C.R. 1343, p. 2, ¶¶ 1-5.

occur as a result of the conspiracy.[87] Holmes' assistance in manipulating Bunnington stock created the foreseeable result that the brokerage houses would sustain losses.[88] Holmes' parking of stock for Lugo created the foreseeable result that the capital troubles of FSSC would be worsened. Therefore, unlike the defendant law firm in *Bloor*, adverse consequences as a result of Holmes' acts and the acts of his co-conspirators were likely if not certain to occur. Plaintiffs therefore present a genuine issue that Holmes' acts, and those of his co-conspirators, created a foreseeable loss to SIPC and the Trustees, further necessitating a reversal of the order of summary judgment.

Holmes cites to *Miller* and argues that the instant case is somehow analogous to the facts in *Miller*. However, even a cursory review of the factual allegations of *Miller* reveals that the last allegedly culpable transaction in that case took place two and one-half years before the damage was sustained. The court held as follows:

> The considerations that are important in applying the "substantial" or "essential" factor test [of proximate cause], such as lapse of time,

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[87] Holmes misleading and erroneously contends that the demise of FSSC and Sebag was, according to Plaintiffs' theory, a "calculated result" of the conspiracy. Opposition Brief, p. 29. Plaintiffs have never ascribed such a plan to the conspiracy. In any event, the demise of FSSC and Sebag were foreseeable consequences of the acts of the conspiracy whether or not intended.

[88] Indeed, FSSC traded on and promoted protection by SIPC by the use of SIPC's logo on trade confirmations and statements. *See e.g.*, C.R. 1317, Exh. 9001. Thus, not only was loss to SIPC in the event of failure foreseeable, but clearly probable and predictable as a result of the failures.

> the number and impact of other factors and the extent to which the defendant's conduct created a continuous and active potential for harm, all counsel against a finding of proximate cause in these circumstances.[89]

Understandably, the district court in *Miller* held that the remote transactions could not have caused harm to the brokerage some two and one-half years later.[90]

In stark contrast, the facts before this Court show that Holmes was involved with the manipulative scheme, invested illicit income into an enterprise, and conducted the affairs of FSSC and Sebag through a pattern of racketeering activity, at the precise time that the firms collapsed. There was no lapse of time between Holmes' overt acts and the loss. Further, Holmes' conduct in manipulating Bunnington stock created exactly the active potential for harm missing in *Miller*. Thus, *Miller* is not valid authority for the summary judgment granted by the District Court.

C. Holmes Is Secondarily Liable For Aiding And Abetting Securities Laws and RICO Violations.

Holmes ignores the substantial evidence that he aided and abetted the target securities manipulations, and is secondarily liable for the acts of his co-defendants also underlying the manipulations. Holmes does not contest the existence of an independent primary wrong, *i.e.*,

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[89] *Miller*, 413 F.Supp. at 1068.

[90] 413 F.Supp. at 1067-68 (S.D.N.Y. 1976).

the manipulation of Bunnington stock;[91] however, Holmes fails to acknowledge that his actual knowledge of the manipulation and "substantial assistance" are uniquely fact-intensive questions inappropriate for resolution on summary judgment.

Both RICO and Rule 10b-5 allow secondary liability based upon a defendant's status as an aider and abettor.[92] Holmes' extensive participation in the affairs of the FSSC-Sebag enterprise, and his affirmative assistance to others in violating RICO and Rule 10b-5, directly undermine the argument that proximate cause has not been shown here. Reversal and remand for trial is therefore appropriate.

V.

THE DECLARATIONS OF EXPERTS FOLEY AND TORKELSON AND PLAINTIFFS' STATEMENT OF BACKGROUND AND FACTS DEMONSTRATE GENUINE ISSUES OF MATERIAL FACT AND WERE PROPERLY CONSIDERED BY THE DISTRICT COURT

Holmes claims that the declarations of Plaintiffs' experts James C. Foley ("Foley") and John B. Torkelson ("Torkelson") (the "Declarations"), and the Statement of Background and Facts (the "Statement"), submitted by Plaintiffs in opposition to Holmes' motions for summary judgment do not satisfy the requirements of Federal Rule

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[91] In fact, Holmes affirmatively asserted below that the Bunnington manipulation caused the collapse of the FSSC and Sebag. *See* C.R. 1281 at 12-13.

[92] *See DCD Programs, Ltd. v. Leighton*, 833 F.2d 183, 188 (9th Cir. 1987) (Rule 10b-5) and *Petro-Tech, Inc. v. Western Co. of North America*, 824 F.2d 1349, 1358-62 (3rd Cir. 1987) (RICO).

of Civil Procedure 56(e), and are therefore inadmissible as evidence.[93]

In his reply to Plaintiffs' Opposition to Motion for Summary Judgment filed in the District Court,[94] Holmes objected to the Declarations on the grounds that they contained impermissible opinions and legal conclusions as to Holmes' motives and failed to attach authenticated copies of documents relied upon.[95] However, the trial court did not exclude any of Plaintiffs' evidence. The documents are properly part of the record before the Court on appeal.

A. The Declarations Are Admissible.

1. Experts May Opine On Ultimate Issues.

Holmes claims that the Declarations do not comply with the requirements of Federal Rule of Civil Procedure 56(e) because the declarants testify as to ultimate facts and conclusions of law, and opine as to Holmes' motives.[96] He also objects to the Declarations on the

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[93] Opposition Brief, pp. 8-13. Although both Declarations state the background, qualifications and expertise of the declarants, Holmes claims that Foley and Torkelson impermissibly testify as to "legal conclusions." The Declarations state that they are offered as the testimony of the experts designated by Plaintiffs, and the opinions and conclusions by Foley and Torkelson are given by persons who are qualified as experts in the customs and practices of the securities industry.

[94] C.R. 1326 at 2-3.

[95] Holmes also objected to the Statement on the ground that it exceeded the maximum number of pages allowed by the Local Rules of Practice. C.R. 1326, pp. 2-3.

[96] Opposition Brief, p. 10.

grounds that the documents referenced by Foley and Torkelson were not attached to the Declarations.[97] Holmes' position is squarely in opposition to the law of the Ninth Circuit.

The cases[98] Holmes relies on to support his claim that Foley and Torkelson impermissibly testify in their Declarations as to legal conclusions, ultimate issues and Holmes' motives are inapplicable here. The cases discuss only the limitations on a *non-expert's* testimony. Holmes' contention that such opinions are barred even where the declarant is an expert, is based on a single district court case from Nevada.[99] The law of the Ninth Circuit is clear, however, that both the permissible scope and substance of an expert's testimony (by declaration or otherwise) are indisputably broader than those of a percipient witness. This increased range of areas on which an expert may testify as to his conclusions and opinions is embodied in Federal Rules of Evidence 703, 704(a) and 705 and is set forth clearly in many Ninth Circuit cases.

For example, in *Bieghler v. Kleppe*,[100] the plaintiffs were injured in a motorcycle accident. The plaintiffs sued the United States, which moved for summary judgment. The plaintiffs opposed the motion and filed the affidavit of an accident reconstruction expert who opined that the accident was caused by defective lighting in a tunnel. On

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[97] *Id.*, p. 9.

[98] *Cermetek, Inc. v. Butler Aupah, Inc.*, 573 F.2d 1370 (9th Cir. 1978); *Washington v. Maricopa County*, 143 F.2d 871 (9th Cir. 1944); *Sanders v. Douglas*, 565 F.Supp. 78 (C.D. Cal. 1983).

[99] *Condos v. Conforte*, 596 F. Supp. 197, 199 (D. Nev. 1984).

[100] 633 F.2d 531 (9th Cir. 1980).

appeal from summary judgment in favor of defendants, the *Bieghler* defendants, like Holmes, contended that the affidavit of plaintiffs' expert was "conclusory, based on hearsay, and not within personal knowledge, and otherwise [contained] inadmissible opinion evidence."[101]

This Court noted that pursuant to Federal Rule of Civil Procedure 56(e), affidavits submitted in support of or in opposition to a summary judgment motion must be " 'made on personal knowledge, . . . set forth such facts as would be admissible in evidence, and show affirmatively that the affiant is competent to testify to the matters stated therein.' "[102] The *Bieghler* Court held, however, that:

> Rules 702, 702, 704, and 705 of the Federal Rules of Evidence dispose of defendants' argument. Rules 702 and 704 allow properly qualified experts to testify in the form of an opinion about issues as to which their expertise may assist the trier of fact, even if the opinion embraces an ultimate issue of fact. Rule 703 permits the expert to base opinions or inferences on facts or data not admissible in evidence if they are of a type reasonably relied upon by experts in the field. Rule 705 permits an expert to give opinion testimony without prior disclosure of the underlying facts or data.
>
> The expert's affidavit here affirmatively showed his qualifications as an expert in accident reconstruction and the study he had undertaken to form his opinions. Although it did not describe in detail how he had arrived at his

[101] *Id.* at 533.

[102] *Id., quoting* Fed. R. Civ. P. 56(e).

> conclusions, the affidavit gave more than a bare conclusion that defendants had been negligent and that their negligence caused the accident.[103]

In *Shad v. Dean Witter Reynolds Inc.*,[104] the Shads brought an action against the defendant brokerage firm and their stockbroker, alleging that their account had been "churned." The trial court allowed Shads' expert to testify only as to "objective" matters such as the definition of churning and to identify trading patterns in the Shads' accounts.[105]

Additionally, the trial court did not allow Shads' expert to state his opinion as to the ultimate issues in the case, whether the trading was excessive and therefore whether the accounts had been churned. The expert was also precluded from testifying regarding "the significance of various types of transactions, whether they were appropriate to the Shads' circumstances and objectives, and whether the making of those transactions evidenced reckless disregard of the Shads' interests."[106] The Shads' expert was similarly prevented from testifying regarding defendants' motives in trading the accounts and from stating the opinion that defendants' only purpose was to earn commissions.[107]

The Ninth Circuit held that it was prejudicial error for the trial court to exclude the opinions of the Shads' expert on the ultimate issues of whether the account had

[103] *Id.*

[104] 799 F.2d 525 (9th Cir. 1986).

[105] *Id.* at 527.

[106] *Id.*

[107] *Id.* at 528.

been churned and whether the broker had acted with reckless disregard or "scienter." This Court found that the Shads' expert should have been allowed to state his opinion on a wide range of issues, including whether the broker "controlled" the account, whether he engaged in "excessive trading" and the issues of "risk, comparative suitability and trading patterns."[108] The Court also authorized the Shads' expert to offer his inferences and conclusions, which he had drawn from the evidence, as to the broker's motives, whether the broker "intended to defraud" the Shads, or whether he acted with "reckless disregard" for their interests because "[s]cienter usually will not be established by direct evidence, but rather will be inferred from a finding of excessive trading and control. The reasons for allowing expert testimony regarding control and excess trading are equally applicable to scienter."[109]

It is thus well established under the law of the Ninth Circuit that, contrary to Holmes' assertion, an expert may state his opinion as to conclusions, ultimate issues and a party's motives or intent.[110] Holmes' objection to the expert affidavits must therefore be overruled.

2. Documents Relied On By An Expert Need Not Be Attached To An Expert's Declaration.

Holmes objects to the Declaration on the basis that the documents referenced by Foley and Torkelson are not

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[108] *Id.* at 530.

[109] *Id.*

[110] *Id.* at 527-30; *Bieghler*, 633 F.2d at 533-34; *See also Bulthuis v. Rexall Corp.*, 789 F.2d 1315, 1318 (9th Cir. 1985); *Pacific Legal Found v. State Energy Resources, etc.*, 659 F.2d 903, 912 n.15 (9th Cir. 1981), *cert. denied*, 457 U.S. 1133 (1982).

attached and authenticated pursuant to Rule 56(e). This objection similarly is without merit. Federal Rule of Evidence 705 provides in pertinent part that "the expert may testify in terms of opinion or inference and give reasons therefor without prior disclosure of the underlying facts or data, unless the court requires otherwise."

In *Bulthuis*, the lower court rejected the affidavits of two doctors in opposition to defendant's motion for summary judgment on the grounds that the doctors failed to state the facts on which their medical opinions were based.[111] This Court found that although the doctors did not describe in detail how they arrived at their opinions, they sufficiently explained that their opinions were based on changes that they had observed in the plaintiff's tissue. In reversing the lower court, the Ninth Circuit held:

> Expert opinion is admissible and may defeat summary judgment if it appears the affiant is competent to give an expert opinion and the factual basis for the opinion is stated in the affidavit, even though the underlying factual details and reasoning upon which the opinion is based are not. If further facts are desired, the movant may request and the district court may require their disclosure. In this case, both experts stated their opinions were based on observed tissue changes and no greater detail was requested. The affidavits should have been considered.[112]

Under Federal Rule of Evidence 705 and the holding of *Bulthuis*, Foley and Torkelson, as experts, were not

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[111] *Bulthuis*, 789 F.2d at 1317-18.

[112] *Id.* at 1315.

required to attach and authenticate the documents. In addition, contrary to Holmes' claim that the referenced documents must be attached and authenticated in order for the testimony concerning or based on such documents to be admissible, Federal Rule of Evidence 703 provides in pertinent part that "[i]f of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence." Moreover, in the proceeding below, neither Holmes nor the District Court requested the presentation of additional factual bases for experts' opinions. The Declarations are therefore admissible.

B. The Statement Of Background And Facts And Its Appendix Of Exhibits Are Properly Part Of The Record.

Holmes objects to Plaintiffs' Statement of Background and Facts on the grounds that it fails to satisfy the requirements of Federal Rule of Civil Procedure 56(e)[113] and that its contents are immaterial to the issues presented by his summary judgment motion.[114]

Holmes claims that the Statement is inadmissible because it does not conform to the requirements of Rule 56(e); however, he also acknowledges that the Statement "is not an affidavit or declaration."[115] Rule 56(e), however, only sets forth the requirements for an affidavit in

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[113] Opposition Brief, p. 8.

[114] *Id.* at 13.

[115] *Id.*

support or in opposition to a summary judgment motion. The Statement is not, as Holmes acknowledges, an affidavit or declaration. It is clearly a narrative exposition of the facts, supported by evidence filed in opposition to Holmes' motions for summary judgment (which is presently in the record before this Court), and is signed by counsel for Plaintiffs as such.

Since the Statement is not an evidentiary document and need not conform to Rule 56(e), what remains of Holmes' objection to the Statement is that it "is a work of historical fiction."[116] The essence of Holmes' objection to the Statement is, therefore, that Plaintiffs have suggested inferences and conclusions based upon the underlying facts concerning Holmes' role in the scheme with which Holmes disagrees. In *Miller v. Schweickhart*,[117] cited by Holmes, the Court discussed the inferences that a fact finder may draw from established facts. The court held that:

> It is recognized, of course, that . . . [the defendant's] categorical denials of wrongdoing are by no means conclusive, and by themselves do not require the granting of defendant's motion for summary judgment. . . . The Court also recognizes that the absence of direct evidence is not fatal to plaintiffs' claim – indeed it is fully aware that conspiracies are rarely established by direct evidence; that usually they are spelled out by independent circumstantial evidence and the reasonable inferences to be drawn therefrom. . . .

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[116] *Id.* at 12.

[117] 413 F. Supp. 1062 (S.D.N.Y. 1976).

> A fact finder may draw reasonable inferences from known or proven facts, but the inference must be based on common experience and be logical or reasonable. . . . [118]

The fact that Holmes interprets the same factual evidence differently than Plaintiffs merely illustrates that there are dramatically different interpretations and conclusions that a fact finder can reasonably draw from the same evidence.

Holmes argues that the Statement does not constitute admissible evidence.[119] Holmes has acknowledged, however, that the Statement was accompanied by eight volumes of exhibits which are referenced in the Statement, and which were designated as part of the record on this appeal.[120]

In addition, Holmes did not object to the admissibility of any of the attached exhibits in the District Court, nor has he raised any objection to the eight volumes of exhibits on appeal. Federal Rule of Evidence 103 provides that "in case the ruling is one admitting evidence, a timely objection or motion to strike [must state] the specific ground of objection if the specific ground was not apparent from the context." No such objection was made and none appears in the record. Judge Wright has described the "well-settled rule that affidavits not in compliance with Rule 56(e) may be considered by the trial court in the absence of an objection by counsel."[121] In the

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[118] *Miller*, 413 F. Supp. at 1065.

[119] Opposition Brief, p. 13.

[120] *Id.*

[121] *United States v. Dibble*, 429 F.2d 598, 603 (9th Cir. 1970) (J. Wright, concurring).

absence of such an objection, the exhibits constitute part of the record on appeal and should be considered by the Court along with the Statement, as they were considered by the District Court.

VI.

CONCLUSION

For the reasons set forth in the Opening and Reply Briefs, and in the SEC's Amicus Curiae Brief, this Court should reverse the order of summary judgment and remand the case for trial. SIPC and the Trustees must be allowed to try their cases against Holmes.

DATED: October 20, 1989

STEPHEN C. TAYLOR
JOEL E. BONNER
MARK D. LARSEN
SHEPPARD, MULLIN,
RICHTER & HAMPTON
G. ROBERT BLAKEY
CORNWELL & BLAKEY
Attorneys for Plaintiff-Appellant Securities Investor Protection Corporation

C. EDWARD SIMPSON
MICHAEL J. ABBOTT
JONES, BELL, SIMPSON &
ABBOTT
Attorneys for Plaintiffs-Appellants Eugene W. Bell Trustee for the Liquidation of Joseph Sebag Incorporated and Laurence A. Schroeder. Successor Trustee for the Liquidation of First State Securities Corporation

PROOF OF SERVICE BY MAIL

STATE OF CALIFORNIA)
) ss.:
COUNTY OF LOS ANGELES)

I am a citizen of the United States and a resident of or employed in the City of Los Angeles; I am over the age of 18 years and not a party to the within action; my business address is 1706 Maple Avenue, Los Angeles, California 90015.

On October 20, 1989, I served the within Reply Brief in re: "Securities Investor Protection Corporation vs. Robert G. Holmes, Jr." in the United States Court of Appeals for the Ninth Circuit, Nos. 89-55094 and 89-55128, on all parties interested in said action, by placing two true copies thereof enclosed in a sealed envelope, with postage thereon fully prepaid, in the United States Post Office mail box at Los Angeles, California, addressed as follows:

Jack I. Samet, Esquire
David H. Bramson, Esquire
Julie B. Haupt,
Attorney at Law
Buchalter, Nemer, Fields
& Younger
700 South Flower Street
Suite 700
Los Angeles, California
90017
Counsel for Defendant:
Robert G. Holmes, Jr.

Michael A. Oswald,
Esquire
Oswald & Yap
5000 Birch Street
Suite 4600
Newport Beach, California
92660
Counsel for Defendants:
Frankie Mae Garrity,
Rodger W. Garrity and
Velma Shaw (aka
Velma Shaw Meyers)

Hugh Steven Wilson,
Esquire
G. Andrew Lundberg,
Esquire

Latham & Watkins
555 South Flower Street
Los Angeles, California
90071
Counsel for Defendants:
Gordon H. McNeil and
Isadore Diamond

James W. Mercer, Esquire
Jeanne E. Irving,
Attorney at Law
Hennigan & Mercer
611 West Sixth Street
28th Floor
Los Angeles, California
90017
Counsel for Defendants:
Magnetic Technologies
Corp.
(Bunnington Corp.)

David L. Ross, Esquire
Greenberg, Traurig, Askew,
Hoffman, Lipoff, Rosen
& Quentel
1221 Brickell Avenue
19th Floor
Miami, Florida 33131
Counsel for Defendant:
Creditbank

Martin N. Gelfand, Esquire
Hockman, Salkin & DeRoy
9100 Wilshire Boulevard
7th Floor
West Tower
Beverly Hills, California
90212
Counsel for Defendants:
Nettie Vigman
and Seymour Vigman

Steven Gourley, Esquire
Feinstin, Gourley
& Mandel
11111 West Olympic
Boulevard
Suite 300
Los Angeles, California
90064
Counsel for Defendants:
Jack Haber, Haberico,
Inc.,
Habers, Inc., and
Habers, Inc., a
Defined Benefit
Pension Trust

Steven P. Rice, Esquire
Kindel & Anderson
555 South Flower Street
29th Floor
Los Angeles, California
90071
Counsel for Defendant:
Aero Systems, Inc.

Lee Huszagh, Esquire
330 Alhambra Circle
Coral Gables, Florida 33134
Co-Counsel for
Defendant:
Aero Systems, Inc.

Stephen H. Marcus, Esquire
Frandzel & Share
8383 Wilshire Boulevard
Suite 400
Beverly Hills, California
90211
Counsel for Defendants:
Dash Industries, Inc.
Jay Dash and Phillip
Dash

William E. Taylor, III,
Esquire
Leonard Dubin, Esquire
Blank, Rome, Comisky
& McCauley
1200 Four Penn Center
Plaza
Philadelphia, Pennsylvania
19103
Co-Counsel for
Defendants:
Dash Industries, Inc.,
Jay Dash and Phillip
Dash

David Stowell, Esquire
David Pash, Esquire
Kinsella, Boesch, Fujikawa
& Towle
1875 Century Park East
Suite 1600
Los Angeles, California
90067
Counsel for Defendants:
Aerosonic Corporation,
Inc.,
Herbert J. Frank
and David S. Goldman

Joseph J. Brigati, Esquire
Jeffery B. Maletta, Esquire
Kirkpatrick & Lockhart
1800 M Street, N.W.
South Lobby
Washington, D.C. 20036
Co-Counsel for
Defendants:
Aerosonic Corporation,
Inc.,
Herbert J. Frank
and David S. Goldman

Sheldon M. Jaffe, Esquire
Law Offices of Sheldon M.
Jaffe, P.C.
1888 Century Park East
Suite 2100
Los Angeles, California
90067
Counsel for Defendant:
Edward P. Prescott

Joel S. Fass, Esquire
Colondy, Fass & Talenfeld
626 N.E. 124th Street
Miami, Florida 33161
Counsel for Defendant:
Elliot I. Eiseman

Jeffrey Allan Tew, Esquire
Kirkpatrick & Lockhart
100 Chopin Plaza
Suite 2000
Miami Center
Miami, Florida 33131-2305
Counsel for Defendant:
Martin Blumenthal

Howard J. Privett, Esquire
Bill E. Schroeder, Esquire
McCutchen, Black, Veleger
& Shea
600 Wilshire Boulevard
Los Angeles, California
90017
Counsel for Defendant:
Jose Luis Calonge
(aka Jose Luis Calonge
Rivas)

Robert C. Gebhardt,
Esquire
2151 LeJuene Road
Suite 310

Coral Gables, Florida 33134
Counsel for Defendant:
Jose Camprubi Sala

Roger Garrity
15292 Nantes Circle
Irvine, California 92714

Frankie Mae Garrity
15292 Nantes Circle
Irvine, California 92714

Mario Lamar
Attorney at Law
Lamar, Lamar &
Associates, P.A.
3971 S.W. 8th Street
Miami, Florida 33134
Counsel for Defendants:
Tula Corporation and
Talingo Corporation

Karla L. Bell,
Attorney at Law
McKittrick, Jackson,
Demarco & Peckenpaugh
4041 MacArthur Boulevard
5th Floor
Newport Beach, California
92660
Co-Counsel for
Defendant:
Martin Blumenthal

Office of the U.S. Trustee
26 Federal Plaza
New York, New York 10278

Richard O'Connell, Esquire
Chapter 7 Trustee
Yost & O'Connell
161-24 Northern Boulevard
Flushing, New York 11358
Chapter 7 Trustee for
Joseph A. Lugo, Jr.

Joseph A. Lugo, Jr.
415 E. 54th Street
New York, New York 10022

Charles Anshen, Esquire
16944 Ventura Boulevard
Encino, California 91316

Stuart D. Perlman, Esquire
30 North LaSalle Street
Suite 2630
Chicago, Illinois 60602

Delores Owens Cipparone
15 N.E. 123rd Terrace
North Miami, Florida 33161
Defendant, *In Pro Se*

Robert Mansell
c/o Huberman Margaretten
& Straus
1380 Miami Gardens
North Miami Beach,
Florida 33179

Rudolph A. Aragon,
Esquire
Coffey, Aragon, Martin and
Burlington, P.A.
2699 S. Bayshore Drive
Penthouse
Miami, Florida 33133
Co-Counsel for
Defendant
Creditbank, Inc.

Jack Corinblit, Esquire
Corinblit, Shapero
& Seltzer
3700 Wilshire Boulevard
Suite 820
Los Angeles, California
90010

Lester L. Levy, Esquire
Wolf Popper Ross Wolf
& Jones
845 West Third Avenue
New York, New York 10022

C. Edward Simpson,
Esquire
Michael J. Abbott, Esquire
Jones, Bell, Simpson
& Abbott
800 Wilshire Boulevard
Fifth Floor
Los Angeles, California
90017

I declare under penalty of perjury that the foregoing is true and correct. Executed on October 20, 1989, at Los Angeles, California.

/s/ Ce Ce Medina
CE CE MEDINA